

NAVAL POSTGRADUATE SCHOOL

MONTEREY, CALIFORNIA



THESIS

**STREAMLINING THE
CONTRACT CLOSEOUT PROCESS**

by

James Valovcin

December 1995

Principal Advisor:

David V. Lamm

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**STREAMLINING THE
CONTRACT CLOSEOUT PROCESS**

James Valovcin
Lieutenant Commander, Supply Corps, United States Navy
B.S., Fairfield University, 1980

Submitted in partial fulfillment
of the requirements for the degree of

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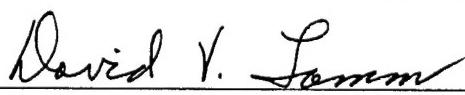
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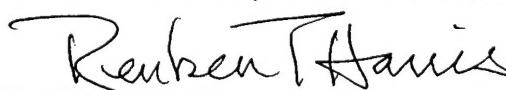
Approved by:



David V. Lamm
David V. Lamm, Principal Advisor



William Gates, Associate Advisor



Reuben T. Harris, Chairman
Department of Systems Management

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I. INTRODUCTION

A. BACKGROUND

The Department of Defense (DoD) budget has been on a declining trend over the last five years. The President and Congress have closely examined the programming and expenditures of Defense spending. Massive Federal budget deficits have been the impetus of severe Department of Defense spending cuts. Many major weapon system programs that were robust in the 1980s are now either drastically reduced or non-existent. As a result, each Service must judiciously examine its budget planning and execution practices in order to be more prudent with the available appropriated funds.

The contract closeout process plays a major function in this equation. Excessive delays in the closeout process increases the Government's exposure to contractors' financial difficulties. Delays in contract closeout also increase the risk of using current year funds to pay for prior year obligations. Other adverse impacts of untimely contract closeout include the misuse of Government-furnished property, possible overpayments to contractors and large backlogs which disrupt the normal flow of work in contracting offices.

The contract closeout process has been under intense analysis over the last few years. Numerous General Accounting Office (GAO), Department of Defense Inspector General (DoDIG) and Service audits have specifically addressed the deficiencies and associated ramifications of this process. As a result of these audits and reports, the Department of Defense has begun to evaluate this process and develop the appropriate improvements. Recently, in October of 1994, the Under Secretary of Defense (Acquisition and Technology)

chartered a Process Action Team that was directed to develop a comprehensive plan to re-engineer the contract administration process. [Ref. 1, p. iii] The contract closeout process was reviewed and several significant procedural changes recommended. Setting in motion these contract administration process improvements can potentially save the Department of Defense millions of dollars and will benefit all individuals and organizations involved in the contracting process. However, the underlying issue with contract closeout remains whether the process is efficiently and effectively managed.

B. INTRODUCTION

Government contracting officers must perform a myriad of duties throughout the contracting phase of the acquisition process. The results of acquisition planning, solicitation, source evaluation, negotiations and contract award all lay the foundation for the events that take place post award. One area that has received a great deal of review and attention over the past ten years is the contract closeout process which occurs during the final contracting phase, contract administration.

There are several issues that contribute to the inefficient execution of the contract closeout. The contract closeout process can be detailed, lengthy and time-consuming. The mechanics of the closeout process and the individuals involved vary by contract type and complexity of the item being procured. Additionally, it seems many contractors have little incentive to accelerate the process and achieve more timely closeout. Factor in lukewarm management attention and it is obvious why this process has gone awry.

The closeout process for a contract generally commences when a contract is physically complete (i.e., the final receipt and acceptance of the material or services ordered). The

administrative closeout process consists of 15 actions listed in the Federal Acquisition Regulation (FAR) 4.805-4, "Detailed Procedures For Closing Out Contract Files." These actions are typically accomplished after the contract has been physically completed and not concurrent with performance. The untimely completion of anyone of these actions generates many potential adverse impacts on the contracting agency.

In a 1993 customer survey, the Defense Contract Management Command (DCMC) identified the contract closeout process to be "one of the most important services provided and one with which customers are least satisfied." [Ref. 1, p 15-2] Effective contract administration should insure that contract closeout is performed on time and in an efficient manner, yet past performance measures indicate otherwise. The need for a strategic management plan that provides sound business policy and guidance has arisen. Contract closeout cycle times and their associated costs must be reduced to an acceptable level that meets the customer's satisfaction.

C. PURPOSE

The primary purpose of this thesis is to review the management of the contract closeout process (primarily within the Defense Contract Management Command and selective Department of the Navy contracting activities) and determine if it is performed in an effective and efficient manner. Secondary objectives are to identify the areas that impede the process and/or are neglected throughout the process and ramifications thereof. Finally, recommendations will be presented for a "streamlined" management approach to the contract closeout process that can be applied throughout the contract administration phase.

D. RESEARCH QUESTIONS

In order to accomplish the objectives of this thesis, fundamental research questions were developed. The primary research question is:

* What are the principal factors that affect the management of the contract closeout process and how can improvements be implemented to streamline the process ?

The following subsidiary questions will be addressed in order to elaborate on the primary question:

- * What are the current procedural requirements for contract closeout ?
- * What are the primary factors affecting timely and proper contract closeout ?
- * What are the consequences to the Government for untimely contract closeout ?
- * What marginal utility/benefit would the Government obtain if contracts were closed-out in a timely manner ?

E. SCOPE AND ORGANIZATION

The main thrust of this thesis will be to examine the management of the contract closeout process and analyze how the process can be streamlined in accordance with the purpose and intent of the Federal Acquisition Streamlining Act and Guiding Principles for the Federal Acquisition System.

The study will focus on the data accumulated from interviews conducted with various Defense Contract Management Command (DCMC) and contractor personnel in an effort to investigate the actual execution of the contract closeout process. The research will analyze the impact of untimely contract closeout actions in an effort to determine what policy and/or procedures should be implemented that would improve the marginal utility of the process.

The thesis will be a case study that will examine the contract closeout process, implementation and execution of these processes and obstacles inherent to the process. Accordingly, recommendations for streamlining this process will be discussed.

The thesis is arranged in five chapters. In this Chapter, background information is presented, the purpose of this research has been defined, the scope and direction of the research identified and methodology for data collection detailed.

Chapter II delineates the procedural requirements of the contract closeout process. It also consists of definitions of terminology germane to the process, individuals involved in the closeout process and time standards for the process.

Chapter III will address past audits of the contract closeout process within various DoD organizations and the adverse impacts of untimely closeout.

Chapter IV presents the data collected via interviews with individuals closely involved with the closeout process and analyzes the salient factors of these data.

Lastly, Chapter V will present conclusions and recommendations for process improvement, answers to the research questions and areas for further research.

F. METHODOLOGY

The primary research methodology employed was an extensive review of the pertinent literature. Additional information from Department of Defense directives and instructions was also examined. This review was conducted to obtain background information and analyze the relevant data on the subject matter. Sources included: the Acquisition Library and the Dudley Knox Library at the Naval Postgraduate School, the Defense Logistics Studies

Information Exchange (DLSIE), the Federal Acquisition Regulation, and various professional publications.

The secondary research methodology utilized was a series of interviews with Administrative Contracting Officers (ACOs), Procuring Contracting Officers (PCOs), Defense Contract Audit Agency (DCAA) auditors and private contractors. This supplements, clarifies and updates various findings from the relevant literature.

The information derived from these sources was reviewed and examined in order to conduct a sound analysis and render an objective appraisal of the subject matter.

II. THE CONTRACT CLOSEOUT PROCESS

A. BACKGROUND

The contract closeout process is frequently considered to finalize numerous actions started during contract administration. The process involves certain contracting actions for an individual (physically completed) contract to be concluded and the file to be marked closed. A contract is deemed physically complete when one of the following conditions exist:

[Ref. 2: p. 7]

- (a) the contractor has delivered all supplies or performed all services required by the contract and the Government has inspected and accepted the supplies or services,
- (b) contract option provisions have expired without being exercised, or
- (c) a contract termination notice has been given to the contractor.

Once a contract is determined to be physically completed, the contracting officer can commence the requisite closeout actions, prepare the final closeout documentation and submit the file to the archives. The process is complex and involves interactions between various contracting organizations.

B. DEFINITIONS

The following general definitions of terms associated with the contract closeout process are provided for a common frame of reference. The definitions were obtained from basic acquisition and contract literature and regulations.

CONTRACT: A term used to describe a variety of legally binding agreements between the Government and a contractor. Consideration is an integral part of the contract. The

contractor agrees to provide goods or services within a specified time-frame, at an agreed to standard of quality, and at an agreed price. In turn, the Government agrees to pay the contractor and perform any other responsibilities required by the contract. [Ref. 3]

CONTRACT CLOSEOUT: The required series of actions taken by the Government (and contractor) to finalize a contract. These actions usually commence after the completion of contractor deliveries or termination and the settlement of all claims and litigation by the Government and the contractor. Finally, the contract is removed from the list of open contracts and the file is marked closed. [Ref. 4]

CONTRACT COMPLETION: The condition that occurs when the contractor has delivered all goods and/or services required by the contract, and the Government has evidence of receipt, inspection and acceptance of the deliveries. Contract completion is generally considered the starting point for the contract closeout process. [Ref. 4]

CONTRACT TERMINATION: Discontinuation of a contract by the Government before the contractor completes performance. Termination can be for default if a contractor does not or cannot meet the contract terms and conditions, or for convenience when the Government has determined the termination is in its best interest. [Ref. 5]

CONTRACTOR: A profit-oriented business or entity, a nonprofit organization, or an individual legally capable of entering into a binding agreement with the Government to provide goods or services. [Ref. 3]

COST-REIMBURSEMENT CONTRACTS: This term refers to a family of pricing arrangements which reimburses allowable, allocable and reasonable costs incurred for contract performance, to the extent that such costs are prescribed or permitted by the contract. These contracts may also include provisions for profit, and for incentive fees or award fees that motivate the contractor to reduce costs and/or improve the quality of performance. Costs incurred generally must be validated by contract administrators and contract auditors prior to final settlement and contractor payment. [Ref. 3]

FINAL PAYMENT: The last payment made to a contractor for performance under a specific contract. Generally, final payment is often preceded by negotiations, contract audit and other contracting actions. [Ref. 4]

FIRM FIXED-PRICE CONTRACT: Contracts for delivery of goods or services at a firm price. The contract price is not subject to adjustment or redetermination based on actual costs or performance of other factors. The price negotiated is the price paid and the contractor is obligated to perform. [Ref. 3]

GOVERNMENT FURNISHED EQUIPMENT/PROPERTY: The generic terms used to describe real estate, equipment, tools and material provided by the Government for use on specific contracts. [Ref. 6]

OBLIGATION: A legal liability for the Government to pay a contractor the amount stated in the contract. Obligations are recorded in the financial accounting records of the Government. Once an obligation is incurred (at contract award), those funds are restricted and cannot be used for any other purpose unless they are deobligated. [Ref.4]

OVERHEAD COSTS: (Indirect Costs) Any cost incurred by the contractor which cannot be directly identified with a single final cost objective but with two or more final cost objectives or with at least one intermediate cost objective. Some common examples include the cost of operating a corporate headquarters, the cost associated with acquiring materials (e.g. purchasing, shipping and receiving), salaries for factory maintenance personnel and salaries of personnel offices. These overhead costs are allocated or prorated to all benefiting projects and contracts and are generally expressed as a percentage of direct or other costs. On cost-reimbursement contracts, overhead costs are subject to validation and audit. Agreement on the final rates often requires negotiations. [Ref. 3]

PARTIAL PAYMENT: A payment authorized under a contract made to a contractor upon completion of the delivery of a portion of the goods and services required, delivered and accepted by the Government under the contract. Partial payment under fixed-price contracts are used to liquidate progress payments. [Ref. 3]

PAYMENTS FOR COSTS INCURRED: These payment are considered a form of contract financing typically used on cost-reimbursement contracts. Contractors can be periodically

(usually monthly) reimbursed for actual costs incurred, pending submission of final invoices for each year's period of performance. Procuring Contracting Officers, Contract Administrators and contract auditors must validate and approve contractors' invoices for costs incurred through onsite reviews and contract audits. The validation and audit of year end invoices determine if the contractors have been over or underpaid and the amount of final payment for each year. [Ref. 3]

PROGRESS PAYMENTS: These payments are considered a form of contract financing used on fixed-price contracts. Contractors can be authorized progress payments when delivery periods exceed six months between the start of the work and first anticipated delivery, contracts exceed \$1 million (\$100,000 for small businesses), and expected contractor expenditures have a significant impact on the contractor's working capital. Contractors can submit monthly invoices and be paid for progress payments based on costs incurred. The progress payments are to be liquidated when invoices for goods or services are presented by the contractor and paid by the Government. Progress payments require validation by the contract administrator and/or auditor personnel. [Ref. 7]

C. PLAYERS INVOLVED IN THE CONTRACT CLOSEOUT PROCESS

The following list delineates the different personnel and organizations that are regularly involved in the contract closeout process:

CUSTOMER: The customer drives the total acquisition and contracting process by defining requirements and forwarding them to the contracting office for execution. Customers can be

program managers for major weapon systems, a material manager directorate for components and spare parts, a research and development directorate or a maintenance and engineering directorate. Customers are responsible for much of the acquisition planning, including early identification of requirements and timely requests for contracting actions placed on contracting officers. [Ref. 4]

PROCURING CONTRACTING OFFICER (PCO): The individual warranted on behalf of the Government, who awards the contract for the Government, closes it out, and is the primary point of contact for all terms and conditions of the contract between the contractor and the Government. The PCO is responsible for all contractual actions and uses a supporting team of specialists which perform many of the actions required in the contracting process and contract closeout. The PCO is independent from the customer and should be able to ensure proper contracting procedures and internal controls are successfully implemented. [Ref. 3]

ADMINISTRATIVE CONTRACTING OFFICER (ACO): The individual delegated certain contractual responsibilities by the PCO. This individual is independent from the customer and is normally assigned to the Defense Contract Management Command (DCMC). They typically employ supporting staffs of engineers, industrial specialists, contract administration specialists, quality assurance specialists, property specialists and other administrative personnel. They perform virtually all contract administration functions, participate in

negotiations with contractors, complete many or most of the contract closeout functions and report on completed transactions and problems to the PCO. [Ref. 3]

FINANCE OFFICE: The Defense Finance and Accounting Service (DFAS) organization records and accounts for all financial transactions relating to contracts. These transactions include obligations, adjustments, disbursements, liquidation of progress payments and interim cost reimbursements, disbursements of final contract payments, collection of debts owed by contractors, and final inventory accounting for Government-furnished property. The finance office also pays all contractor invoices based on receipt of adequate supporting documentation and approvals. The finance office maintains a file for each contract and closes out the file when all financial transactions are completed. [Ref. 4]

CONTRACT AUDITORS: The individuals who perform all audits required of contractor costs. The audits can include review of contractors' cost proposals, actual costs incurred, contractors' accounting procedures, internal controls, economy and efficiency of operations and program results and the potential for defective pricing by contractors. Normally, contract audits are done by personnel of the Defense Contract Audit Agency (DCAA). [Ref.]

D. INSPECTION AND ACCEPTANCE

Inspection and acceptance are primary steps to ensure that the supplies and services acquired under Government contract conform to the contract's quality and quantity requirements. [Ref. 8] They are also an integral part of the contract closeout process. It is

essential that the Government confirm the inspection and acceptance of supplies and services before the contract closeout process begins.

Inspection, as defined in the FAR, means examining and testing supplies or services (including, when appropriate, raw materials, components, and intermediate assemblies) to determine whether they conform to contract requirements. Acceptance means the act of an authorized representative of the Government by which the Government, for itself or as an agent of another, assumes ownership of the existing identified supplies tendered or approves specific services as partial or complete performance of the contract. [Ref. 9]

The contract should specify the location of both inspection and acceptance; at source or destination. Verification of inspection and acceptance is one way to provide evidence that a contract is physically completed, which in turn, commences the closeout process. The absence of either inspection or acceptance will delay contract closeout if these requirements are cited in the contract.

E. CONTRACT CLOSEOUT PROCESS AND REQUIREMENTS

The procedural requirements for the contract closeout process are delineated in the FAR. [Ref. 10] The administrative closeout process will typically commence once the cognizant contract administration office has evidence a contract is physically complete. The process begins with an initial contract funds status review in order to identify and inform the contracting office if excess funds are available on the contract. Once this action is completed, the administrative closeout procedures commence in which the ACO will ensure that, if applicable, the:

- * Disposition of classified material is completed;
- * Final royalty report is cleared;
- * There is no outstanding value engineering change proposal;
- * Plant clearance report is received;
- * All interim or disallowed costs are settled;
- * Price revision is completed;
- * Subcontracts are settled by the prime contractor;
- * Prior year indirect cost rates are settled;
- * Termination docket is completed;
- * Contract audit is completed;
- * Contractor's closing statement is completed;
- * Contractor's final invoice has been submitted, and
- * Contract funds review is completed and deobligation of any excess funds is recommended.

Although the ACO initiates these steps, the PCO is responsible for completing the final step: contract funds review and deobligation of excess funds.

Once the above actions have been verified, the next step in the administrative closeout process calls for the ACO to prepare a Contract Completion Statement, DD Form 1594.

[Ref. 10] Some of the pertinent information contained in this statement include:

- * Contract administration office name and address (if different from the contracting office);
- * Contracting office name and address;
- * Contract number;

- * Last modification number;
- * Last call or order number;
- * Contractor name and address;
- * Dollar amount of excess funds, if any;
- * Voucher number and date if final payment has been made;
- * Invoice number and date, if the final approved invoice has been forwarded to a disbursing office or another agency or activity and the status of the payment is unknown;
- * A statement that all required contract administration actions have been fully and satisfactorily accomplished;
- * Name and signature of the contracting officer; and
- * Date the contract completion statement was signed.

Upon completion of this statement, the ACO will forward the signed original to the contracting office for placement in the contract file. In addition, a signed copy is placed in the contract administration file.

The final step of the contract closeout process involves the storage and disposition of the contract files. The FAR states that agencies shall prescribe procedures for the handling, storing and disposing of contract files. [Ref. 11] In addition, this reference also specifies retention periods for certain contractual documents.

F. SPECIFIC CONTRACT REQUIREMENTS

Several of the fifteen contract closeout requirements are invoked through a contract clause while the others are procedural requirements. Each contract should be reviewed to determine the applicability of certain clauses or procedures that will ultimately effect the

contract closeout process. The following synopses delineate the actions required by these clauses and procedures:

Classified Material: Classified materials are disposed of in accordance with procedures approved by the Defense Industrial Security Office. Disposition instructions should be specified in the contract. The three most common ways for handling the disposition of classified materials are: retain the material, return it to the Government, or properly destroy it. The cognizant contracting officer should be consulted if the disposition instructions are not specified.

Royalties (FAR 52.227-9): Royalties refer to any costs or charges in the nature of royalties, license fees, patent or license amortization costs, or the like, for using or for rights in patent and patent applications. The contractor is required to furnish a statement of royalties paid or required to be paid in connection with the performance of the contract and subcontracts, including reasons why the royalties are necessary.

Value Engineering Change Proposals (FAR 52.248-1): Value engineering is the formal technique by which contractors suggest methods for performing their actions more economically. The contractor will share in the savings. The alternative methods are submitted to the Government in the form of a Value Engineering Change Proposal (VECP). The contractor shall submit VECP's to the contracting officer unless otherwise stated. The PCO then notifies the contractor of the status of the VECP within 45 calendar days after

receipt. A VECP may be accepted, in whole or in part, by a contract modification. Contracts with pending VECP's cannot be closed out.

Plant Clearance Report (FAR 52.245-2): Final accounting and disposition of GFP consists of the following actions: Upon completing the contract, or at an earlier date fixed by the PCO, the contractor shall submit inventory schedules covering all items of GFP (including scrap) not consumed in performing the contract or delivered to the Government. The contractor prepares for shipment, delivers or disposes of the GFP as directed by the PCO. The net proceeds of any such disposal are credited to the contract price or paid to the Government as the PCO directs. The Plant Clearance Report addresses all the actions relating to the screening, redistribution, and disposal of the contractor inventory.

Subcontracts: Subcontract claims and issues may impact the prime contract. The ACO must ensure that all subcontracts are completed and settled prior to the prime contract settlement. Field audits or administrative oversight should be used to monitor the process.

Indirect Rates (FAR 52.216-7): The contractor is required to submit to the cognizant contracting officer, within 90 days of the completion of their fiscal year, its final indirect cost rates for that period. Supporting cost data specifying the contract and subcontract should be included. The appropriate Government representative and contractor shall establish the final rates as soon as practical. The parties will execute a written understanding that sets forth the final indirect cost rates. The understanding specifies (1) the agreed-upon final annual indirect

cost rates, (2) the bases to which the rates apply, (3) the periods for which the rates apply, (4) any specific indirect cost items treated as direct costs in the settlement, and (5) the affected contract and/or subcontract, identifying any with advance agreements or special terms and the applicable rates. Failure to agree on a final annual indirect cost rate shall be a dispute subject to the Disputes clause.

Final Payment (FAR 52.216-7): The contractor is required to promptly submit a completion invoice or voucher after completing the work. It must be submitted no later than one year from the completion date. Upon approving that invoice, and when the contractor complies with all the terms and conditions of the contract, the Government will promptly pay any balance of allowable costs and that part of the fee (if any) not previously paid.

G. QUICK CLOSEOUT PROCEDURES

The Quick-closeout procedure is available to expedite the closeout process of cost-type contracts when there will be a delay in the final determination of indirect costs by DCAA. The procedure enables the ACO, under certain circumstances, to negotiate the settlement of indirect costs under a specific contract in advance of final indirect cost rate determination.

The FAR [Ref. 12] provides the circumstances under which the Quick-closeout procedures may be used:

- (1) The contract is physically complete;
- (2) The amount of unsettled indirect cost to be allocated to the contract is relatively insignificant. Indirect cost amounts will be considered insignificant when-

(i) The total unsettled indirect cost applicable to any one contract does not exceed \$500,000.00; and

(ii) Unless otherwise provided in agency procedures, the cumulative unsettled indirect costs to be allocated to one or more contracts in a single fiscal year do not exceed 15 percent of the estimated, total unsettled indirect costs allocable to cost-type contracts for that fiscal year; and

(3) Agreement can be reached on a reasonable estimate of allocable dollars.

There are two important facets of this procedure. First, the determination of indirect costs under the Quick-closeout procedure shall be final for the specific contract it covers and no adjustments shall be made to other contracts for over- or under- recovering of costs allocated or allocable to the contract covered by the agreement. Second, the indirect cost rates used in the Quick-closeout of a contract shall not be considered a binding precedent when establishing the final indirect cost rates of other contracts.

H. TIME STANDARDS FOR CONTRACT CLOSEOUT

Specific time frame requirements for closing out contract files, based on the contract type and value, are as follows: [Ref. 13]

(1) Small purchase files should be considered closed when the contracting officer receives evidence of receipt of property and final payment, unless otherwise specified by agency regulations.

(2) Files for all firm-fixed-price contracts other than small purchases should be closed within 6 months of the month in which the contracting officer receives evidence of physical completion.

(3) Files for contracts that require settlement of indirect cost rates should be closed within 36 months of the month in which the contracting officer receives evidence of physical completion. (This includes fixed-price incentive contracts since they require settlement of contractors' overhead rates).

(4) Files for all other contracts should be closed within 20 months of the month in which the contracting officer receives evidence of physical completion.

The contractors also have specific time frames that must be met in order to facilitate the closeout process. Although these timeframes are delineated in the acquisition regulations, they should be incorporated into the contractual vehicle as a requirement for the contractor.

Some specific timeframes are:

* Final annual overhead rates should be submitted to the Government for review and audit within 90 days of the close of the business year.

* Final invoices on cost-reimbursement contracts should be promptly submitted to the Government when work is completed, but no later than one year after the completion date.

J. SUMMARY

The actions required in the contract closeout process range from simple and quickly executed to difficult and time consuming. The timeframe standards to complete the closeout process are based on contract type. However, the 15 specific actions delineated in the FAR do not have any time standards associated with their execution. The interactions of the various activities involved in contract closeout add to the intricacies of the process. Generally, the difficulty of the closeout process is a function of the dollar value of the contract, type of contract and the complexity of the terms and conditions.

III. CAUSES AND IMPACTS OF UNTIMELY CONTRACT CLOSEOUT

A. INTRODUCTION

The contract closeout process has been under review for over ten years. The Office of the Inspector General, General Accounting Office and Service agencies have all scrutinized this process in an effort to determine whether it is executed in an effective and efficient manner. Universally, they have determined that the contract closeout process is an area that is not performed in an efficient manner and requires greater management attention. The consequences of the inefficient execution of this process are extremely significant and detrimental. The remainder of this chapter will present excerpts from selective reports that are offered to illustrate these points.

B. CAUSES OF UNTIMELY CONTRACT CLOSEOUT

The Army was one of the first organizations to issue details on the closeout process in Advisory Report: HQ 86-A2, Contract Closeout Process of 18 December 1985. The purpose of this report was to furnish Army managers and contracting personnel with a single text that could serve as an instructional document that presents most of the requirements of the closeout process. The impetus for the report was evident: [Ref: 2, p: 4]

The audit found that for the 10 major weapon system contractors audited, the Army had 7,708 open contracts valued at \$35.7 billion as of 31 August 1985. Of these, 2,654 contracts (34.4 percent) valued at about \$6.5 billion (18.2 percent) were overdue for closeout. The time used for closeout exceeded the allowable closeout time frames. The delays in closing these contracts with the 10 contractors ranged from a few months to 8 years.

Findings of this nature provided the motivation for most all Government agencies to evaluate the closeout process and emphasize its importance within contract administration.

Virtually every audit report pertaining to contract closeout has diagnosed the process in detail. As a result, the mechanics of the process have been intensely examined. The primary focus of these audits has been to evaluate the reasons why the process has gone awry. It is imperative that upper-level managers recognize the root causes that disrupt the closeout process.

The following reasons were prevalent throughout the research literature as the main causes of untimely contract closeout:

* **LOW PRIORITY**

The FAR requires the cognizant contract administration office to perform a wide variety of duties. The successful execution of these duties depends on the relative priority placed upon them and the resources allocated to them. Many of the audits found that contract closeout was considered to be a low priority task after performance.

The Army's Advisory Report provides some meaningful insight concerning the reasons for untimely contract closeout: [Ref: 2, p: 4]

Some of the delays were caused by contractors and Defense activities. But Army contracting offices were the major contributor to the delays. The contracting offices generally gave the contract closeout process and required closeout actions low priority. Contracting personnel did not consider closeout to be an important part of the contracting process and did not understand the adverse effects of delayed closeout.

Additionally, survey results from a recent research paper reiterate this "Low Priority" reason:

[Ref: 14, p. 66]

Low priority and limited manpower were the number one reasons provided in the survey for not initiating the closeout process as soon as the contract is physically completed. These two reasons go hand-in-hand; management allocates personnel to functions with a high priority, whereas a function with a low priority does not receive the attention and personnel resources needed to complete the job.

* INACTION BY THE CONTRACTOR

The contractor is required to perform certain actions to facilitate the contract closeout process (e.g., settle all subcontracts, submit final indirect cost rates, submit GFP inventory schedules). Any inaction on the contractor's part may jeopardize the timely closeout of the contract as evidenced in the findings of one audit report: [Ref: 2, p. 12]

Contractors contributed to delayed contract closeout for all types of major weapon system and installation-level contracts. Delays were found in submitting overhead data, negotiating overhead rates and contract prices, submitting draft and final invoices, and responding to queries from contracting offices. ...there are still no incentives for the contractor to achieve timely closeout.

Other research studies have found that contractors have little incentive to accelerate the process and achieve more timely contract closeout if they do not anticipate receiving additional payment. Rather, the contractor places importance on being awarded contracts vice the administrative paperwork associated with the closeout of contracts. [Ref. 14, p. 67]

* INACTION BY DCAA

DCAA plays an integral part in the contract closeout process. Before any Cost-Reimbursement or Fixed-Price- Incentive contract can be closed out, the year end Overhead rates must be audited by DCAA and negotiated by the ACO. Any delay by DCAA in

accomplishing their audit function will adversely impact the closeout process as was found to be the case in one audit report: [Ref. 2, p.11]

The Defense Contract Audit Agency has been slow in completing audits of contractor overhead for many contracts. We identified elapsed times of 3 to 67 months for contract audits, with average times of 19 months, for the contracts audited. Senior managers at the Defense Contract Audit Agency attributed these delays to a shortage of audit personnel. (New recruits) will be used to reduce the backlog of overhead and other cost-incurred audits and should help reduce the time required to close out cost-reimbursement and fixed-price incentive contracts.

Survey reply findings of a recent research paper discovered many of the same reasons as described above: [Ref. 14, p. 69]

DCAA's reason for its tardiness is twofold. One is lack of manpower. With the budget cuts, DCAA must get by with less auditors. With less auditors, DCAA takes longer to fulfill all of its duties. The manpower problem is intensified by the high turnover rate of personnel. A DCAA auditor stated that 'Not only do we have less auditors, but the auditors are inexperienced and need training and assistance in auditing contractors'.

The second reason for DCAA's tardiness in determining the final indirect cost is the low priority that is placed on final overhead audits. Determination of overhead rates is one of their lowest priorities. ...more importance is placed in getting contracts awarded and funds obligated than in determining final overhead rates and de-obligating funds.

The magnitude of this problem is illustrated by a DoDIG Audit which found: [Ref. 15, p. 5]

... the backlog of Defense Contract Audit Agency (DCAA) audits has increased the audit waiting time beyond the 36 months allowed for the entire cost-type contract. Audit findings revealed that 'DCMDM had almost 13,000 contracts, valued at almost \$3.7 billion, awaiting audit before they could be closed.' ...The excessive time delayed contract closeout.

* LACK OF INTERNAL CONTROLS

Internal controls consist of the policies, procedures and/or management information systems in place within an organization that are used to monitor, control and obtain feedback

concerning the effectiveness of various processes. The lack of an effective internal control system may result in a process operating out of its intended parameters with no corrective action implemented.

In June 1987, a continuing audit was conducted by the Army Office of the Auditor General to determine whether the contract closeout process properly protected the interests of the Army. Audits of this nature were conducted at all of the Army's major material commands. The findings and recommendations as a result of this audit addressed the problems in achieving timely contract closeout and the ineffective execution of requisite closeout procedures: [Ref: 2 p: 20]

Closeout was overdue for many of the contracts audited for 15 to 60 months, with some delays up to 99 months, because Army contracting offices were not completing all actions that could be taken to close out contracts promptly. Actions such as obtaining missing documents, resolving questions about missing receipts, recovering government-furnished property, and deobligating excess funds were delayed or not completed. For many contracts, the contracting offices were not aware of the need for corrective action because they did not have a system for identifying actions needed to close out individual contracts.

* INACTION BY THE ACO

The ACO is responsible for executing the majority of the closeout actions required by the FAR. Additionally, the ACO must coordinate the actions of various organizations (e.g., DCAA, contractor, buying office and paying office) involved in the contract closeout process and ensure that each agency has completed the required actions and submitted the appropriate documentation. Any delay on the part of the ACO will ultimately delay the contract closeout process.

The Department of Defense, Inspector General conducted audits from September 1989 through January 1991 of the administration of the contract closeout process within several components of the Defense Contract Management Command. The objectives of these audits were to determine the timeliness of the contract closeout process, validity of unliquidated obligations on the contracts awaiting closeout and the internal controls over the closeout process. The majority of the shortcomings found in previous audits were still rampant: [Ref: 14, p: ii]

DCMDM did not closeout contracts in a timely manner. Delays in contract closeout created a backlog of about 11,700 overage contracts with an estimated \$166.2 million in unliquidated obligations.

The DoDIG cited inaction by the ACOs as a major reason for untimely contract closeout : [Ref: 14, p: ii]

Administrative Contracting Officers did not make required fund reviews on 86 percent of the physically completed contracts reviewed to determine whether the contracts had unliquidated obligations that could be released and reused for other purposes. As a result, \$3.5 million could have been deobligated, but was not. In addition, there were overstated obligations of \$36.9 million and understated disbursements of \$7.3 million.

The findings and recommendations of these audits regularly listed inaction on the part of the ACO as the reason the closeout process was not effective. ACOs did not make required fund reviews on physically complete contracts or were late in recovering overpayments to contractors. These factors were the major cause of untimely contract closeout.

C. IMPACTS OF UNTIMELY CONTRACT CLOSEOUT

Timely contract closeout is the primary step to ensure the Government's best interests are protected. On the contrary, untimely contract closeout action(s) can potentially pose a

variety of adverse impacts upon the Government. The prudent manager should comprehend the magnitude of these impacts and recognize their ramifications. Although the majority of these adverse impacts are readily apparent, others are not as evident or easily understood. The following list provides some of the detrimental impacts of delayed contract closeout:

* MONETARY IMPACT

The monetary impact of untimely contract closeout can be one of several outcomes: unliquidated obligations, negative unliquidated obligations and unnecessary interest costs. Each of these areas will be addressed as a separate issue.

Unliquidated Obligations: Appropriated funds are available for obligation for a definite period; annual or multi-year. (e.g., Operations & Maintenance funding: one year, Procurement funding {excluding Shipbuilding}: three years). These funds are considered obligated once they are placed on contract. The funds become expended when the contractor receives payment. Fund balances are available to make obligation adjustments for a period of two years after an appropriation succeeds its period of availability.

Unliquidated obligations are those unused and unneeded funds that remain on a physically completed contract after some portion of the obligated funds have been expended. Timely deobligation would permit the reprogramming of these funds to satisfy unfunded budget contingencies. However, these funds can potentially be lost if delayed contract closeout actions cause funds to be deobligated after they have expired. This matter is further magnified by the Appropriation Act of FY 1991. The Act changed the way expired funds and "M" accounts are handled. Essentially, the "M" accounts, which were used to collect and hold expired funds for possible future contract payments and adjustments, will no longer exist.

The new regulations place specific time limits on the availability and use of appropriated funds. Once the time limit passes, all balances are canceled and any outstanding obligation must be charged to a current appropriation.

The following examples detail the profound amounts of unliquidated obligations on physically completed contracts:

Excess funds, totaling about \$1.5 million from 5 contracts, were not deobligated. Deobligations were delayed for up to 54 months, and the excess funds could not be reused. For at least 6 other contracts, Army management did not know if excess funds were obligated because of differences between Army accounting records and those of the Defense Contract Administration Service. [Ref. 2, p. 8]

Procuring and Administrative Contracting Officers did not complete contract funds review for 107 of 137 contracts reviewed. Funds reviews were not accomplished at closeout because the FAR listed funds review as the 15th step in the closeout process even though funds reviews were not dependent on the other steps being accomplished. As a result, we identified \$14.9 million (28 contracts) in unliquidated obligations excess to contractual requirements... [Ref. 16, p. 3]

Negative Unliquidated Obligations: As previously discussed, Congress appropriates funds that are used to pay the Government's commitments. Control procedures are in place to ensure an organization does not spend more money than appropriated. Obligations are recorded when an agency enters into a contract. These obligations are liquidated when payments are made. Typically, the amount paid should be equal or less than the amount obligated. In theory, unliquidated obligations should never be negative; in reality, negative unliquidated obligations have reached large dollar values.

There are three primary causes for negative unliquidated obligations: [Ref. 17, p. 9]

- * the contractor was paid too much;
- * a wrong appropriation account was cited when payment was made; or
- * obligation, payment or collection information was inaccurately or incompletely processed.

As a result, both the Air Force (\$54.2 million) and Army (\$19.4 million) have experienced significant negative unliquidated obligation balances that have been unchanged for over a year past physical completion.

Untimely contract closeout actions will permit negative unliquidated obligations to go unchecked. Timely contract closeout actions, specifically contracts funds review, can potentially identify and correct these problems before they reach monumental proportions. Additionally, timely contract closeout actions can conceivably prevent any violation to the Antideficiency Act which prohibits agencies from obligating or expending more funds than the Congress has appropriated.

Interest Costs: In conjunction with the adverse effects caused by negative unliquidated obligations, delayed contract closeout can result in unnecessary interest costs to the U.S. Treasury if the excess payments to contractors are not recovered in a timely manner.

There are three major reasons why contractors are overpaid: [Ref. 17 , p.11]

- (1) contract modifications decrease the contract price and related obligation below the amount already paid to the contractor,
- (2) duplicate payments are made for the same invoice, and
- (3) progress payments are made to contractors before work is actually completed when the final payment is made to the contractor.

These overpayments tie up funds that can otherwise be used to satisfy other unplanned or unfunded requirements. Additionally, the overpayments become interest-free loans to the contractors while simultaneously contributing to the interest on the national debt. Delayed contract closeout actions will prevent the prompt identification and collection of the overpayments.

* **GOVERNMENT-FURNISHED PROPERTY:**

Government-Furnished Property (GFP) refers to that property, material or equipment directly acquired by the Government and subsequently made available to the contractor for use on a particular contract. Contractors are responsible and liable for the GFP in their possession unless otherwise provided in the contract.

Delayed contract closeout can cause GFP to needlessly remain in the possession of contractors which increases the potential for loss, damage or abuse of the property. This is evidenced by an Army audit which found discrepancies of more than \$930,000 between the amount of GFP given to contractors and the amount recovered by the Army. Recovery of this property was delayed for up to 53 months due to untimely contract closeout. [Ref. 2, p. 8] Prompt contract closeout will ensure the timely return of GFP to Government control and not in the contractor's plant where the potential exists for needless acquisition of similar property.

* INCREASED BACKLOG:

Delayed contract closeout actions typically create work backlogs in contracting organizations. These backlogs can disrupt the normal operations of the organization as evidenced when management shifts resources to reduce the backlog. The intensive and extraordinary efforts applied is usually of a short-fused nature. This type of effort causes operating errors and internal control failures. Additionally, many contracting offices resort to diverting personnel from other contracting functions in order to clear the backlog which adversely impacts the normal administrative function of the organization. [Ref. 4, p. 8]

* FRAUD OR WASTE:

Fraud or waste can exist for individual contracts and are often discovered during contract closeout. The detection and resolution of problems such as contractor cost mischarging and defective pricing may be delayed when closeout actions are late. An Army audit report observed the following: [Ref. 2, p. 3]

The Vice Chief of Staff informed us of incorrect cost charging by a contractor that occurred during the mid-to late 1970's but was not discovered until early in 1985 because contract closeout was late. If such long delays are prevalent, Army management cannot expect to detect contractor fraud occurring in 1987 until 1994 or 1995. In turn, this length of delay could be viewed as a coverup.

Additionally, if fraud or waste is eventually discovered, personnel from outside the defense acquisition community may perceive the delay in contract closeout as an attempt to mask acquisition and contracting dilemmas. The perception of impropriety may be damaging to the agency and could result in an attempt to reduce funding. [Ref. 4, p. 8]

* OTHER:

Some other significant impacts of untimely contract closeout include:

- * Legal Claims: Legal claims against both the Government and contractor tend to be minimized when contract closeout actions are completed in a timely manner. Timely contract closeout tends to promptly identify and resolve potential areas of conflict. [Ref. 18, p.13]
- * Records storage: Punctual contract closeout actions, including the disposition of records, will ensure organizations do not physically maintain an excess amount of contract records on hand. The presence of excess records awaiting closeout actions may result in certain files being misplaced or lost.

D. SUMMARY

This chapter presented the causes of delayed contract closeout (low priority, inaction by the contractor, inaction by DCAA, lack of internal controls and inaction by the ACO) and the impacts thereof (monetary impact, Government-Furnished Property, increased backlog and fraud or waste). In order to fully understand the adverse impacts of untimely contract closeout, one must be aware of the consequences. Only through an intensive process review can one develop and implement effective and efficient controls that provide measurable benefits.

The next chapter will present and analyze the data regarding the current execution of the contract closeout process within various DCMC and Navy organizations.

IV. DATA PRESENTATION AND ANALYSIS

A. INTRODUCTION

This chapter presents and analyzes the data that were collected from a questionnaire and interviews conducted by the researcher. The questionnaire was sent to 50 different commands within the DCMC organization and various Department of the Navy procuring activities. Twenty-nine questionnaires were completed and returned to the researcher.

The objective of the questionnaire was to assess (i) the frequency of occurrence of each of the fifteen contract closeout steps listed in the FAR and (ii) the level of difficulty associated with performing these steps. The responses were provided for both Fixed-Price and Cost-Type contracts. Follow-up questions were asked to determine the following:

- * The current priority of the contract closeout within the organization;
- * The level of internal controls used to facilitate and manage the contract closeout process;
- * Specific areas that impede the organizations ability to closeout contracts in the required time frames; and
- * Areas and tasks that can be implemented to improve the current process.

B. CONTRACT CLOSEOUT QUESTIONNAIRE

The FAR delineates fifteen steps that must be considered when a contract is to be closed. The questionnaire asked the respondents to rate the frequency with which their organization performed these functions during the closeout process and the difficulty associated with performing the corresponding procedure. A one (1) through five (5) rating scale was utilized.

The degrees of differentiation are provided in Table 1 below:

SCALE	FREQUENCY	DIFFICULTY
1	Never	Easy
2	Approximately 25 %	Moderately easy
3	Approximately 50 %	Average
4	Approximately 75 %	Moderately difficult
5	Always	Difficult

Table 1. Rating Scale.

The following data are the results from the ratings given to the fifteen closeout actions as they relate to Fixed-Price contracts and Cost-Type contracts. Appendix A provides a numerical break-out of the responses for the Frequency and Difficulty ratings obtained from the questionnaire. Charts are presented to illustrate the number and range of responses for each closeout function. Additionally, statistical data will be provided to further characterize the data results. An overall assessment of the results will follow the data presentation.

1. Disposition of Classified Material. Figures 1 and 2 show the frequency and difficulty results for the disposition of classified material.

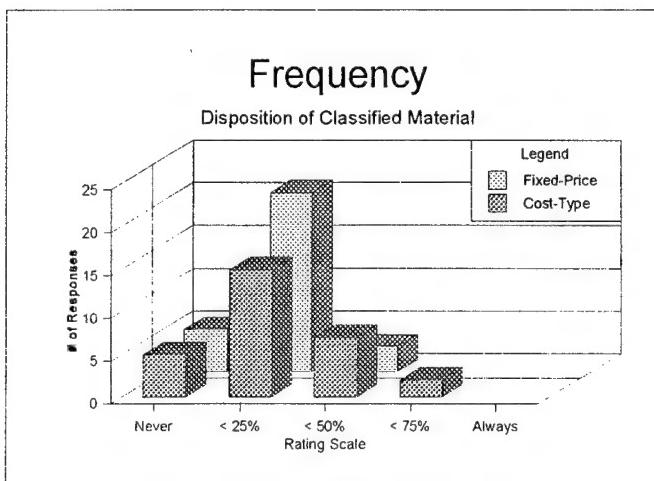


Figure 1.

Fixed-Price

Range: Never to < 50%.

Mean: 1.93 (25% -)

Median: 2 (25%)

Cost-Type

Range: Never to < 75%.

Mean: 2.21 (25% +)

Median: 2 (25%)

Fixed-Price

Range: Easy to Difficult.

Mean: 2.42 (Mod Easy +)

Median: 2 (Mod. Easy)

Cost-Type

Range: Easy to Difficult.

Mean: 2.54 (Average -)

Median: 2 (Mod. Easy)

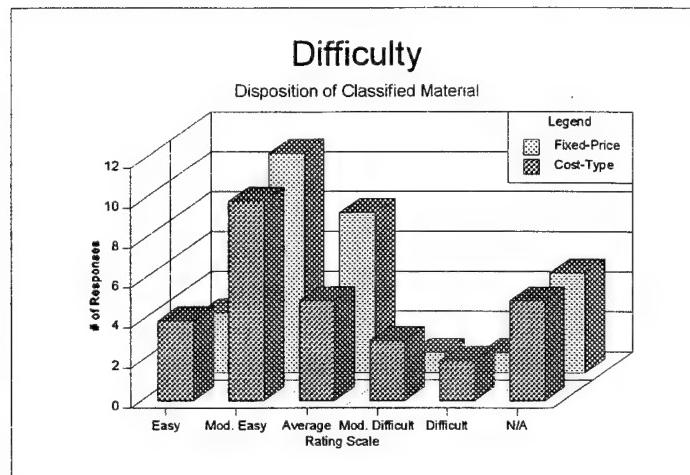


Figure 2.

Assessment: The frequency of this procedure is a direct function of the amount of classified material utilized on a contract. The responding agencies indicated they perform this function approximately 25% of the time for both contract types. Figure 1 shows a rough similarity in the distribution of responses which indicates that there would be no reason this task occurs more often in the contract closeout process for one contract type over the other.

The difficulty assessment can be directly linked to (i) the level of classified material, (ii) the amount of classified material used on the contract, and (iii) the interaction among the ACO, contractor and agency that provides the disposition instructions. Most of the ACOs surveyed considered this task above average in difficulty when the classified material is "Top Secret" and/or there is a great deal of classified material needing disposition. Contrarily, the difficulty was assessed as moderately easy (or below) when the classified material was "Confidential" and the amount was minimal. Figure 2 shows this task to be of moderate ease for Fixed-Price Contracts and average difficulty for Cost-Type contracts.

2. Final Patent Report Cleared. Figures 3 and 4 show the frequency and difficulty of clearing the Final Patent Report.

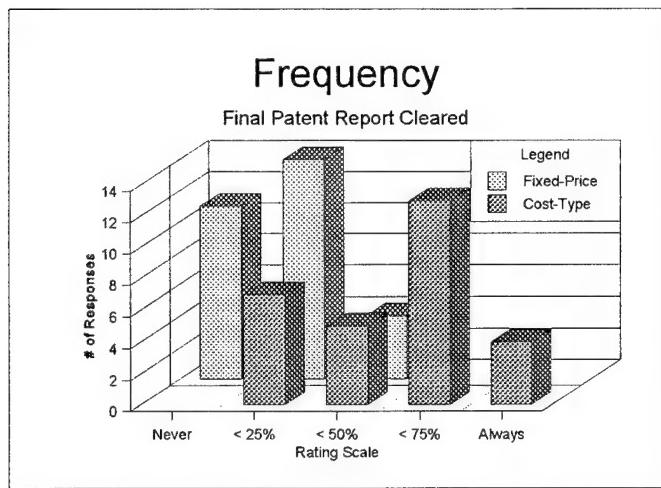


Figure 3.

Fixed-Price

Range: Never to < 50%.

Mean: 1.76 (25% -)

Median: 2 (< 25%)

Cost-Type

Range: < 25% to Always.

Mean: 3.48 (50% +)

Median: 4 (< 75%)

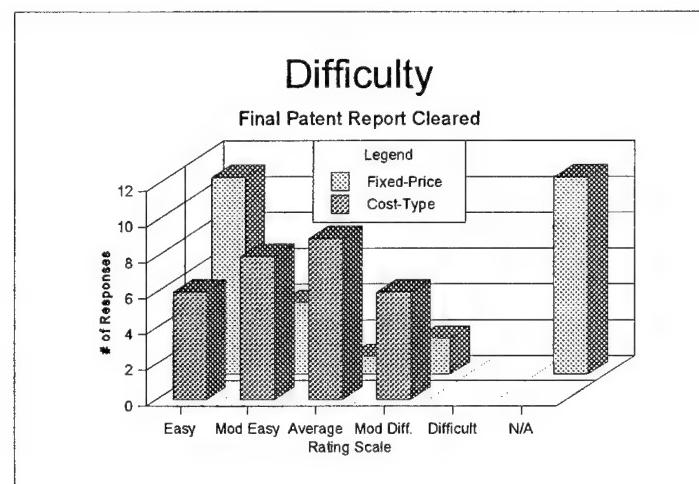


Figure 4.

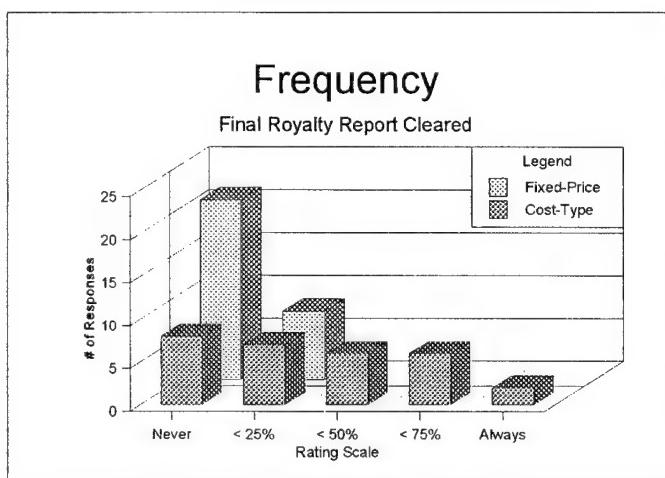
Assessment: Figure 3 shows a disparity in the frequency of performance of this task between the two contract types. Other than production contracts which may produce a patent, Fixed-Price contracts for routine supplies or services would not normally have patent-rights actions. Cost-Type contracts may have a higher incidence of frequency of performance since this contract type is typically used for

Research and Development efforts in which a contractor may produce an invention that requires a patent.

The difficulty of this task depends on the obstacles the ACO may encounter while receiving the patent report. The contractor is required to submit a final patent report within three months after contract completion identifying and listing all inventions produced during the course of the contract, or certify that there were no such inventions. If the contractor fails to notify the Government of the above circumstances, the contracting officer may withhold part of the contract value and cannot release final payment until the report is received. Any untimely reports could adversely impact the contract closeout process.

Figure 4 shows a disparity in the responses to the level of difficulty associated with this task. The contract type and frequency of performance may contribute to the assessment of difficulty associated with this task as it is performed during contract closeout. Since patent reports occur more frequently on Cost-Type contracts, there is a greater chance of receiving late or incomplete reports. This may account for the higher assessment of difficulty for Cost-Type contracts versus Fixed-Price contracts.

3. Final Royalty Report Received.



Fixed-Price

Range: Never to < 25%.

Mean: 1.28 (Rarely)

Median: 1 (Never)

Cost-Type

Range: Never to Always.

Mean: 2.55 (50% -)

Median: 2 (< 25%)

Figure 5.

Figures 5 and 6 show the frequency and difficulty of receiving the Final Royalty Report.

Fixed-Price

Range: Easy to Average.

Mean: 1.75 (Mod. Easy -)

Median: 2 (Mod. Easy)

Cost-Type

Range: Easy to Mod. Difficult.

Mean: 2.14 (Mod. Easy +)

Median: 2 (Mod Easy)

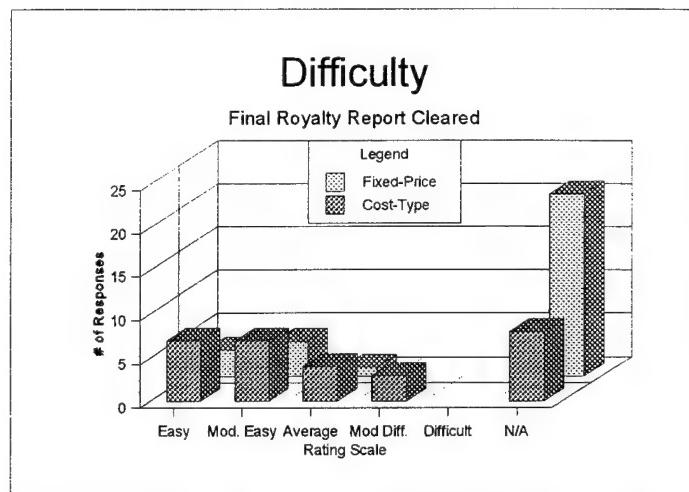


Figure 6.

Assessment: Figure 5 shows the results for frequency are disproportional for the contract types. This task is rarely performed for Fixed-Price contracts but is usually performed for Cost-Type contracts. This may be attributed to the nature of the contract types; Fixed-Price being for stable, less risky requirements where a Cost-Type contract is used for higher risk, more technical needs in which the propensity for a royalty is greater.

The difficulty of this task, as depicted in Figure 6, is concentrated around the Moderately Easy range for both contract types. The contractor is required to notify the contracting officer of royalties paid in connection with performing the contract along with the reasons the royalties are necessary before final payment can be made. Since this task affects final payment, the contractor should be motivated to act in a timely manner. In addition, the Royalty Report may be considered a relatively easy administrative task that does not cause the ACO major problems during contract closeout.

4. No Outstanding VECPs. Figures 7 and 8 show the frequency and difficulty of insuring no VECPs are outstanding.

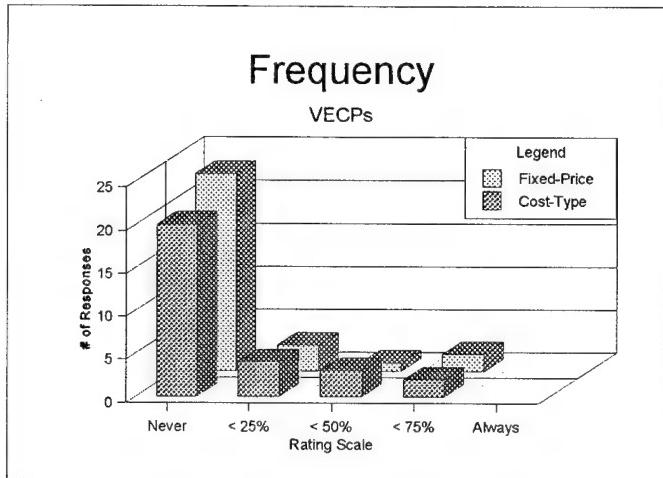


Figure 7.

Fixed-Price

Range: Never to < 75%.

Mean: 1.38 (Rarely)

Median: 1 (Never)

Cost-Type

Range: Never to < 75%.

Mean: 1.55 (25% -)

Median: 1 (Never)

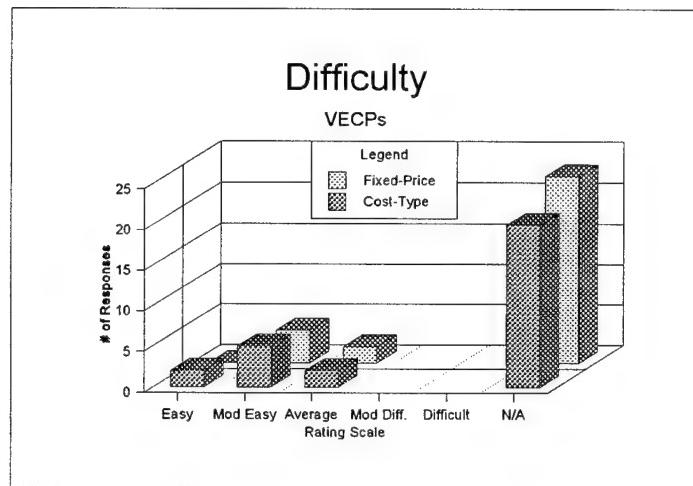


Figure 8.

Assessment: Figures 7 and 8 shows the responses for both frequency and difficulty are similar for both contract types. The results indicate that VECPs typically are not an issue for both contract types when it is time to closeout the contract. This may indicate (i) that the VECP process is efficient and timely, or (ii) the incidence of VECP submittals is low.

When the ACO does contend with VECP issues as part of contract closeout, their resolution was assessed to be of moderate ease. This may be due to the fact that the ACO handles VECP processing as part of routine contract administration and therefore is familiar with the process if it is required at the time of contract closeout.

5. Plant Clearance Report Received.

Figures 9 and 10 show the frequency and difficulty of receiving the Plant Clearance Report.

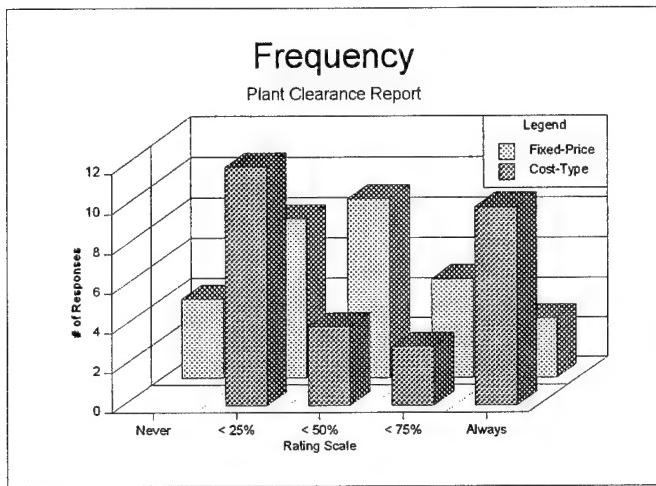


Figure 9.

Fixed-Price

Range: Never to Always.

Mean: 2.83 (50% -)

Median: 3 (50%)

Cost-Type

Range: < 25% to Always.

Mean: 3.38 (50% +)

Median: 3 (50%)

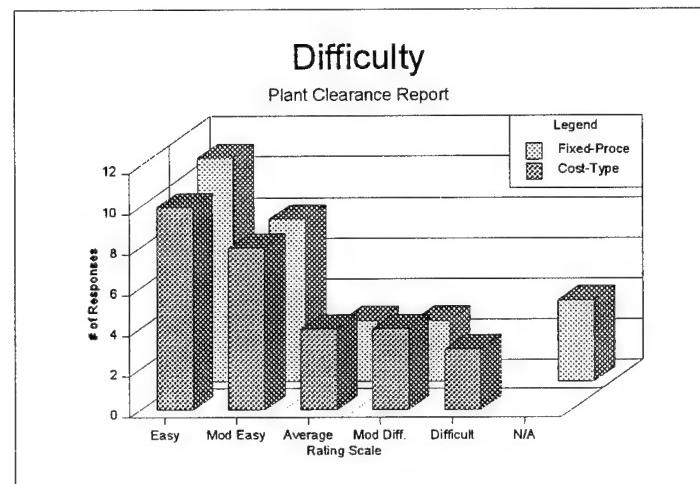


Figure 10.

Assessment: Due to the similarity between Plant Clearance Report and Property Clearance Report, assessment of this task will be deferred to the following subsection.

6. Property Clearance Report Received.

Figures 11 and 12 show the frequency and difficulty of receiving the Property Clearance Report.

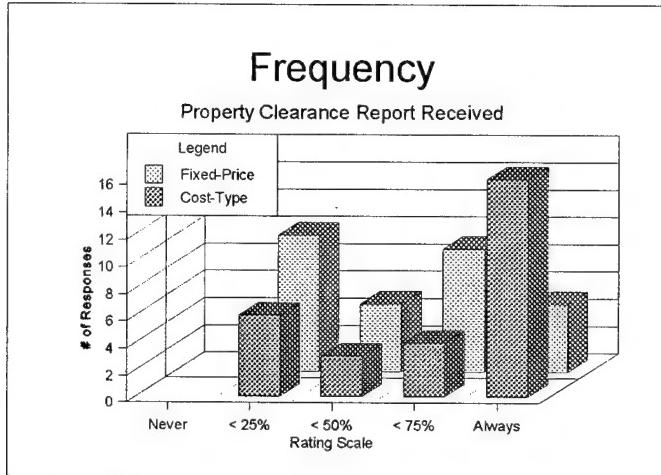


Figure 11.

Fixed-Price

Range: < 25% to Always.

Mean: 3.31 (50% +)

Median: 3 (50%)

Cost-Type

Range: < 25% to Always.

Mean: 4.38 (75% +)

Median: 5 (Always)

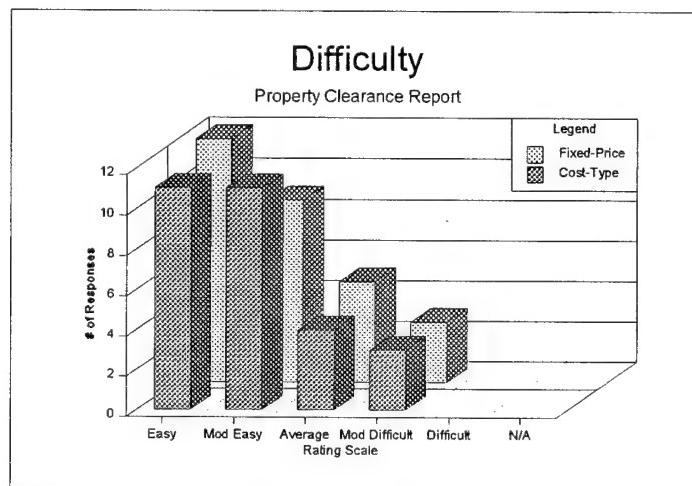


Figure 12.

Assessment: The frequency of performance for this task is directly related to the amount of plant equipment and/or GFP assigned to the individual contract. The average responses for both Plant Clearance and Property Clearance Reports Received, as shown in Figures 9 and 11, imply that these tasks are performed on a regular basis for both contract types.

The difficulty assessment associated with performing these tasks as part of the closeout process is a function of (i) the contractor's plant/property administrator, (ii) the Government's plant/property administrator, (iii) the ACO, (iv) the PCO, (v) the condition of the plant equipment and/or GFP, and (vi) the extent of the disposition action. Figures 10 and 12 indicate these tasks are performed with moderate ease which would indicate the interaction between the listed individuals is usually efficient and effective. Additionally, since plant/property administration are ongoing processes throughout contact administration, the effects on the contract closeout process should be minimal unless they were performed in an inefficient manner.

7. Interim/Disallowied Costs Settled.

Figures 13 and 14 show the frequency and difficulty of settling Interim/Disallowied costs.

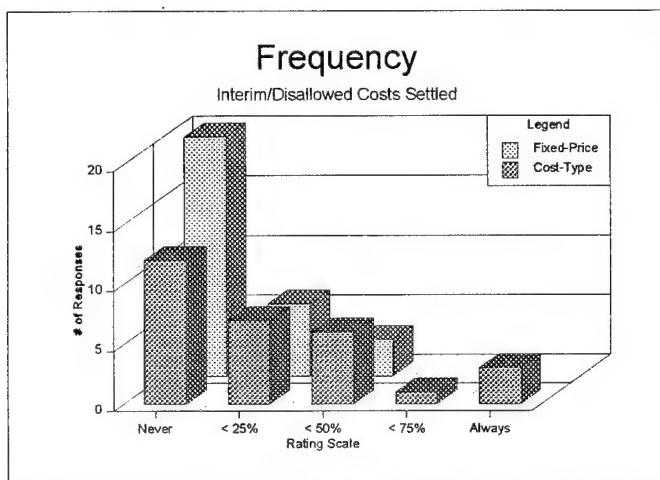


Figure 13.

Fixed-Price

Range: Never to < 50%.

Mean: 1.41 (Rarely)

Median: 1 (Never)

Cost-Type

Range: Never to Always.

Mean: 2.17 (25% +)

Median: 2 (25%)

Fixed-Price

Range: Mod. Easy to Average.

Mean: 2.78 (Average)

Median: 3 (Average)

Cost-Type

Range: Avg. to Mod. Difficult.

Mean: 3.65 (Mod. Difficult -)

Median: 4 (Mod. Difficult)

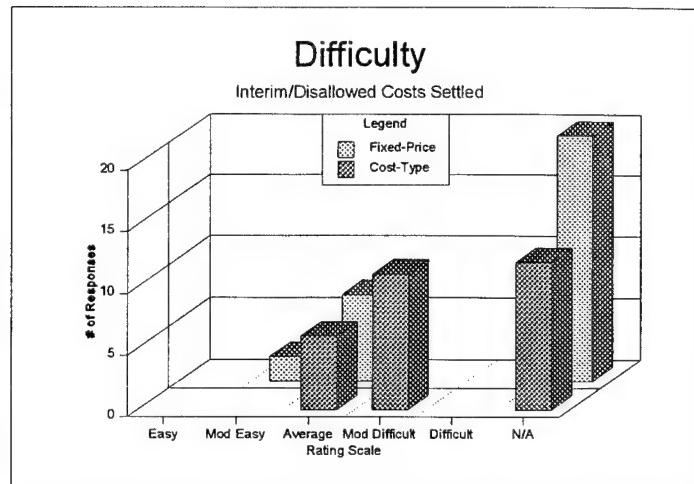


Figure 14.

Assessment: The frequency of this procedure depends upon (i) Contract type, and (ii) whether interim and/or disallowed costs are issues that need to be resolved. This task should be performed for all Cost-Type contracts and Fixed-Price Incentive contracts. This task is not applicable to Firm-Fixed-Price contracts. Figure 13 shows this step is performed relatively infrequently during the contract closeout process for Fixed-Price contracts and of nominal frequency for Cost-Type contracts.

The difficulty of this task is related to (i) the magnitude of the interim and/or disallowed costs, (ii) the timeliness and accuracy of DCAA audit support, and (iii) extent of the negotiations between the ACO and contractor. Figure 14 shows that the majority of responses indicated this task is above average in difficulty for both contract types. This could mean that any of the above related factors have hindered the process and thus made the performance of this task more complicated.

8. Price Revision Completed.

Figures 15 and 16 show the frequency and difficulty of completing the contract price revision.

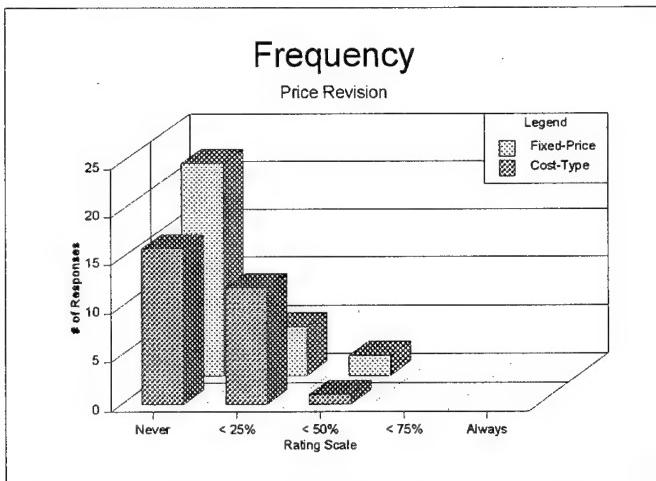


Figure 15.

Fixed-Price

Range: Never to < 50%.

Mean: 1.31 (Rarely)

Median: 1 (Never)

Cost-Type

Range: Never to < 50%.

Mean: 1.48 (Rarely)

Median: 1 (Never)

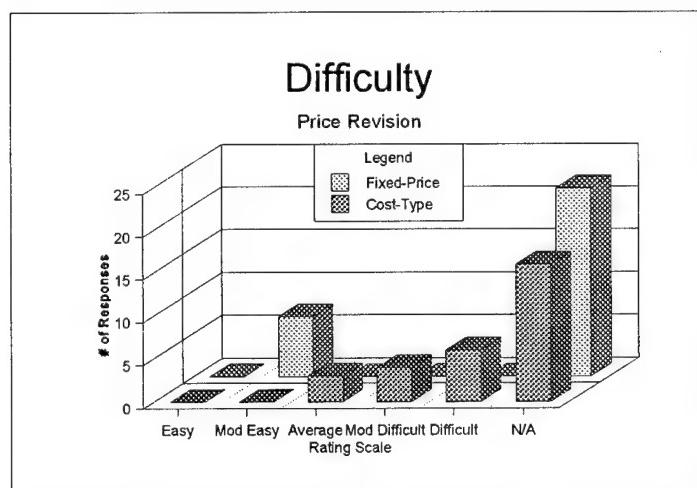


Figure 16.

Assessment: This task is performed when the contract price requires amending due to any circumstances that would increase or decrease the overall contract price (e.g., Economic Price Adjustment or price incentive). Figure 15 indicates that this task is rarely performed during contract closeout for Fixed-Price contracts (since this pricing action is not applicable to Firm-Fixed-Price contracts for contract closeout) and relatively infrequently for Cost-Type contracts.

There is a wide variation in the responses of the assessment of difficulty for each contract type. Figure 16 shows price revision actions were deemed to be of moderate ease for Fixed-Price contracts while Cost-Type contracts were considered to be moderately difficult. The disparity may be attributed to the rigors associated with the audit, analysis and negotiations of costs that are inherent in Cost-Type contract price revisions.

9. Subcontracts Settled by Prime.

Figures 17 and 18 show the frequency and difficulty with insuring the subcontracts are settled by the prime.

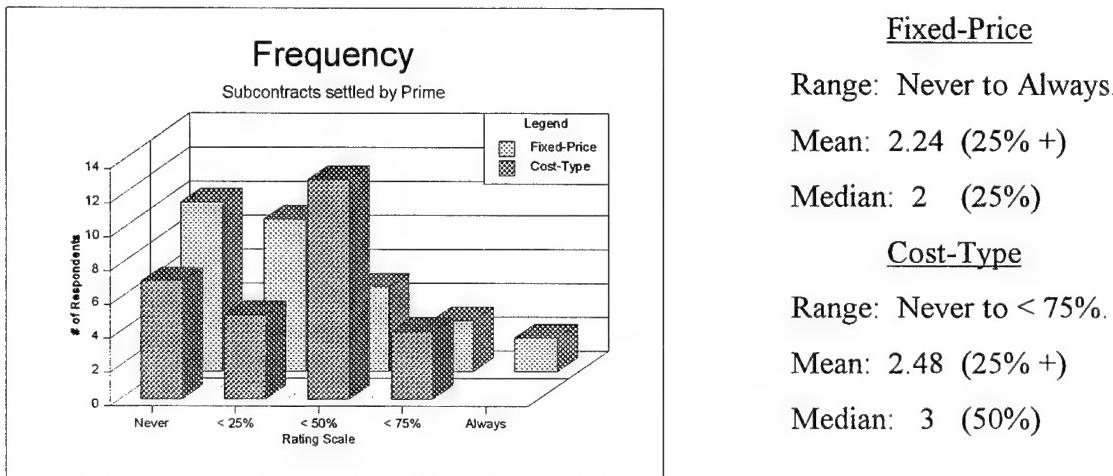


Figure 17.

Fixed-Price
Range: Easy to Mod Easy.
Mean: 1.58 (Mod. Easy -)
Median: 2 (Mod. Easy)

Cost-Type
Range: Mod. Easy to Difficult.
Mean: 3.32 (Average +)
Median: 3 (Average)

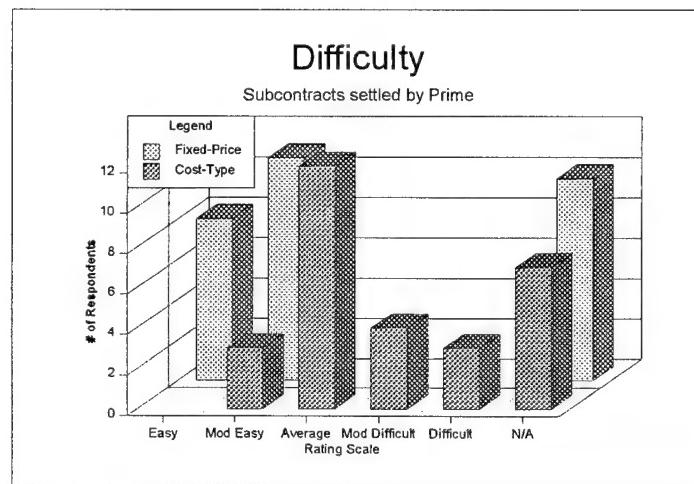


Figure 18.

Assessment: This procedure is only required to be performed as part of the contract closeout process when the prime contractor has subcontracted part of the effort. The responses shown in Figure 17 indicated that this task is performed more often on Cost-Type contract closeout actions. This may be due to the mitigation of risk by the prime contractor under a Cost-Type contract in which some part of the effort is subcontracted.

The difficulty in performing this procedure is a function of the amount of subcontracts the prime contractor has issued and how well the prime contractor administers and settles these contracts. Figure 18 shows the difficulty rating was assessed to be higher for Cost-Type contracts. This may be attributed to the fact that cost-reimbursement subcontracts need to be settled prior to settling final costs for the prime contractor. Additionally, subcontractor claims or issues may add to the degree of difficulty associated with this task.

10. Prior Year Indirect Cost Rates.

Figures 19 and 20 show the frequency and difficulty with settling prior year indirect cost rates.

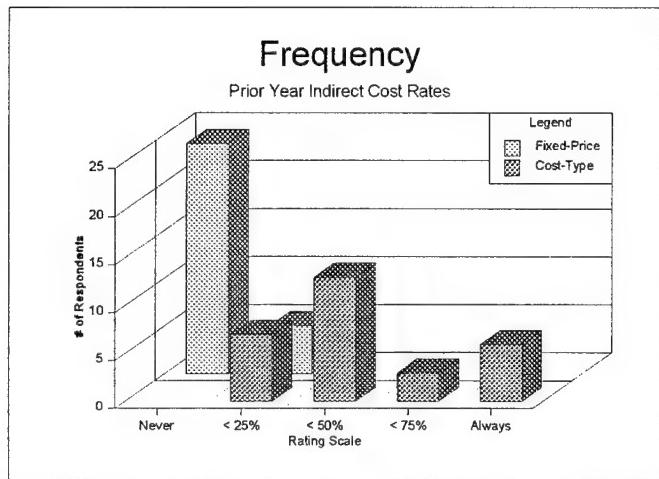


Figure 19.

Fixed-Price

Range: Never to < 25%.

Mean: 1.17 (Rarely)

Median: 1 (Never)

Cost-Type

Range: < 25% to Always.

Mean: 3.28 (50% +)

Median: 3 (50%)

Fixed-Price

Range: Average to Mod. Difficult

Mean: 3.40 (Average +)

Median: 3 (Average)

Cost-Type

Range: Average to Difficult.

Mean: 4.21 (Mod Difficult +)

Median: 4 (Mod Difficult)

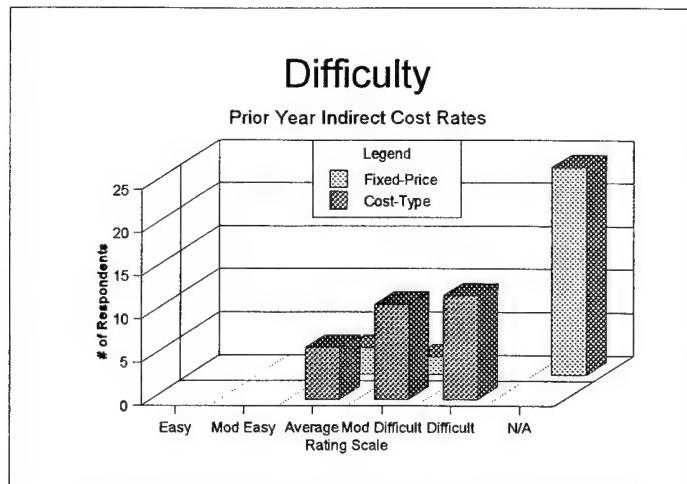


Figure 20.

Assessment: This task is performed on those contracts that require Indirect Cost Rate negotiation (e.g., Fixed-Price Incentive and Cost-Reimbursement). This task is not applicable to Firm-Fixed Price contracts. Figure 19 indicates the performance of this task as part of the contract closeout process is relatively infrequent for Fixed-Price contracts while performance for Cost-Type contracts is relatively frequent.

The difficulty of this task, as shown in Figure 20, is average for Fixed-Price contracts whereas Cost-Type contracts were assessed to be of moderate difficulty. This can be attributed to the following factors: DCAA audit backlogs and delays, settlement of corporate or divisional rates or settlement of subcontractor rates. The settlement of final overhead rates is a crucial element in the closeout of Cost-Type contracts. Since this task is complex, the process may take several years to complete. Until the final rates are established, the Government reimburses the contractor at billing rates established by the contracting officer. These rates are subject to adjustment once the final rates have been established. These factors contribute to the intricacy and difficulty of this process as it pertains to contract closeout.

11. Termination Docket Completed.

Figures 21 and 22 show the frequency and difficulty of completing the termination docket.

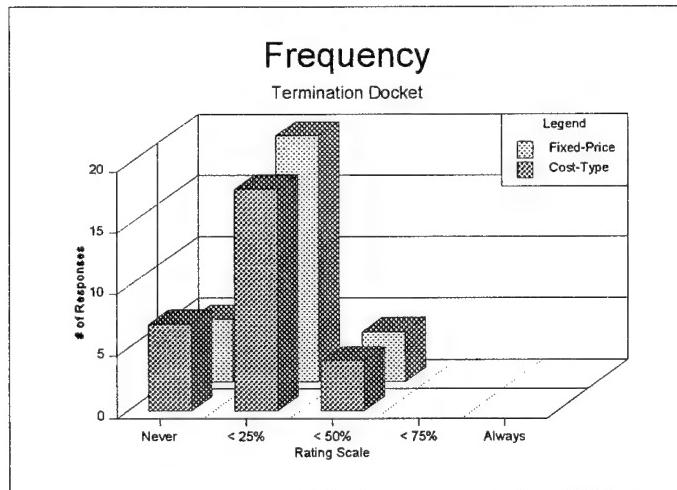


Figure 21.

Fixed-Price

Range: Never to < 50%.

Mean: 2.07 (25% +)

Median: 2 (25%)

Cost-Type

Range: Never to < 50%.

Mean: 1.90 (25% -)

Median: 2 (25%)

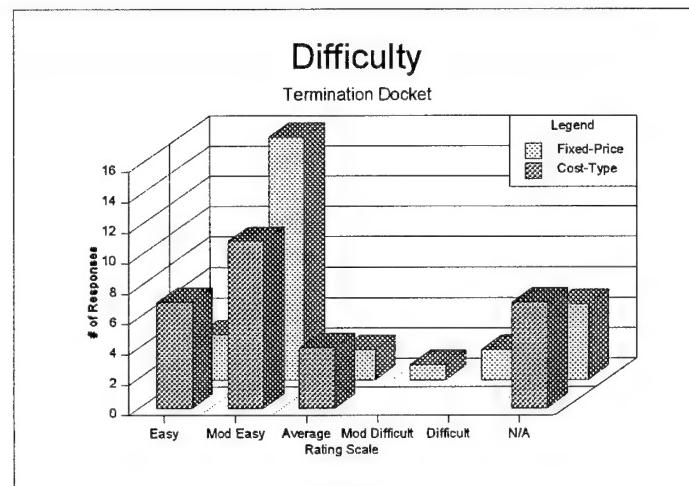


Figure 22.

Assessment: The performance of this task during the contract closeout process is directly related to the amount of termination actions, either for default or convenience, issued by the PCO. The responses show a similar distribution in frequency for both contract types. Figure 21 indicates this function is performed approximately 25% of the time for both Fixed-Price

and Cost-Type contracts. This frequency may be attributed to budget cuts and program reductions which cause an increase in the incidence of termination for convenience actions on behalf of the Government.

The difficulty of this task is directly associated with the actions that must be taken once a termination noticed has been issued. If a contract is terminated for default (T for D), the contractor may be required to transfer title and deliver to the Government any completed or partially completed supplies. The Government will pay contract price for these items. If a T for D was issued and later found to be excusable, then it shall be treated as a termination for convenience (T for C). Under a T for C, the contractor is required to submit a settlement proposal, settle subcontractors' claims and dispose of the termination inventory. The Government will then make the contractor "whole" by reimbursing the contractor for all reasonable and allocable costs incurred in conjunction with performance, as well as reasonable profit on the work completed. The contractor may also recover certain post-termination costs and settlement expenses.

Figure 22 shows that Fixed-Price contracts were rated slightly more difficult on average than Cost-Type contracts. This may be attributed to the dynamics a T for C has on a Fixed-Price contract. A Fixed-Price contract is essentially converted to a Cost-Type contract under a T for C. All reasonable, allocable and allowable costs will be negotiated as part of the settlement. Since these actions are inherently performed under a Cost-Type contract, the T for C would not be as difficult for this type of contract versus a Firm-Fixed-Price contract.

12. Contract Audit is Completed.

Figures 23 and 24 show the frequency and difficulty of completing the contract audit.

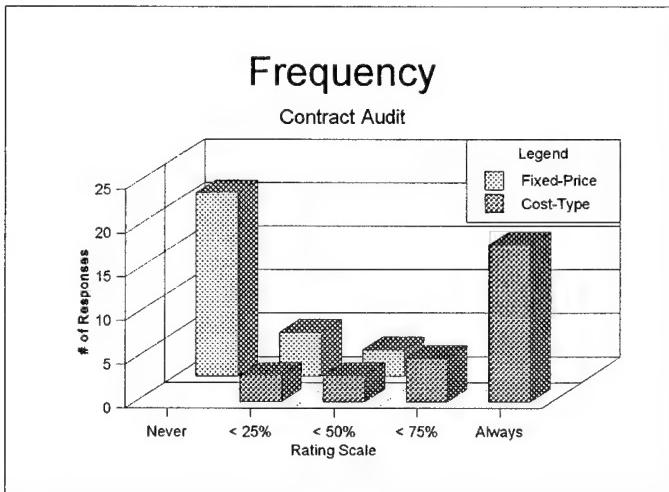


Figure 23.

Fixed-Price

Range: Never to < 50%.

Mean: 1.38 (Rarely)

Median: 1 (Never)

Cost-Type

Range: 25% to Always.

Mean: 4.31 (75% +)

Median: 5 (Always)

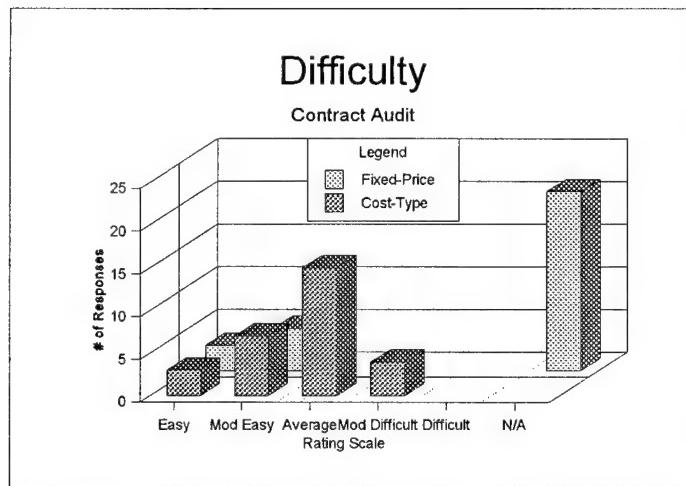


Figure 24.

Assessment: The Government possesses broad audit rights that are derived from the audit clauses included in contracts. The rate at which this right is exercised in the contract closeout process depends on whether this task is required before final payment is made. A contract audit is typically not performed for a Firm-Fixed-Price contract since the price negotiated is

the price paid. The responses shown in Figure 23 indicate that this procedure is rarely performed for Fixed-Price contracts while it is almost always performed for Cost-Type contracts.

The difficulty of this task can be attributed to the magnitude of the records that must be audited, complexity of the contractor's cost accounting system and DCAA audit timeliness and accuracy. The results, as shown in Figure 24, indicate that the audit of Fixed-Price contracts is easy while Cost-Type contracts were deemed to be of average difficulty. This may be due to the additional administrative efforts required to oversee and audit Cost-Type contracts.

13. Contractor's Closing Statement is Completed.

Figures 25 and 26 show the frequency and difficulty of obtaining the Contractor's Closing Statement.

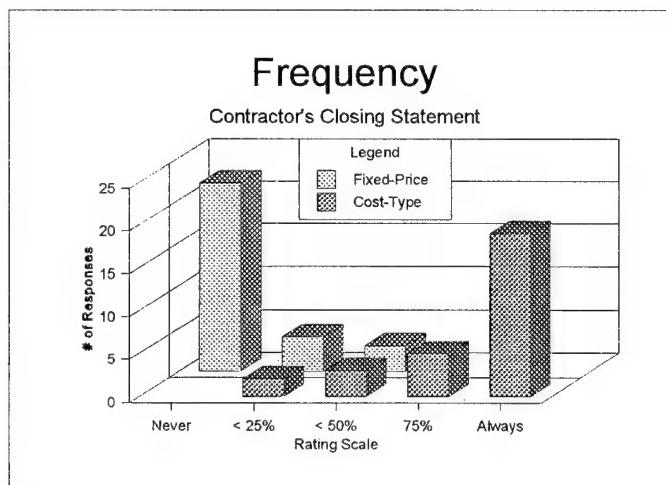


Figure 25.

Fixed-Price

Range: Never to < 50%.

Mean: 1.35 (Rarely)

Median: 1 (Never)

Cost-Type

Range: <25% to Always.

Mean: 4.48 (75% +)

Median: 5 (Always)

Fixed-Price

Range: Easy to Mod. Easy.

Mean: 1.71 (Mod. Easy -)

Median: 1 (Easy)

Cost-Type

Range: Easy to Mod. Difficult.

Mean: 2.79 (Average -)

Median: 3 (Average)

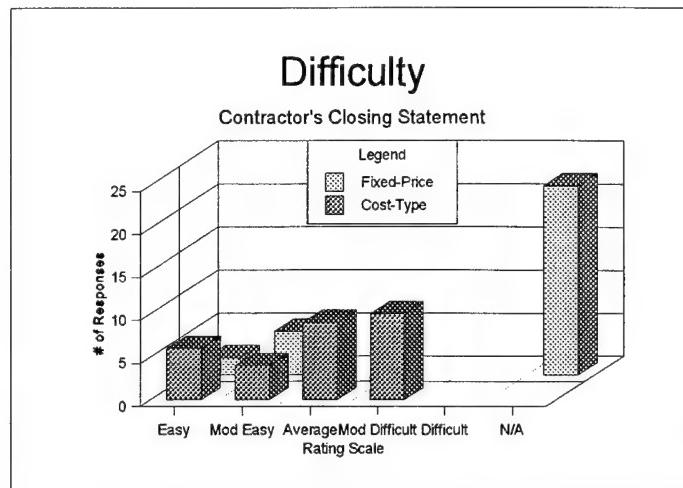


Figure 26.

Assessment: This action requires the contractor to advise the Government that the contract is completed (final acceptance of all deliverable items is completed) and is ready to be processed for closeout. Figure 25 shows that this happens infrequently for Fixed-Price contracts and almost always for Cost-Type contracts.

The difficulty associated with this task is a function of the responsiveness of the contractor. If the contractor submits this statement in a timely manner, then this procedure would be considered easy. However, this task would be appraised as difficult if the contractor submits either inaccurate or untimely statements. The responses shown in Figure 26 indicate Fixed-Price contracts were assessed to be of moderate ease while Cost-Type contracts were deemed average in difficulty.

14. Contractor's Final Invoice Submitted.

Figures 27 and 28 show the frequency and difficulty of receiving the Contractor's Final Invoice.

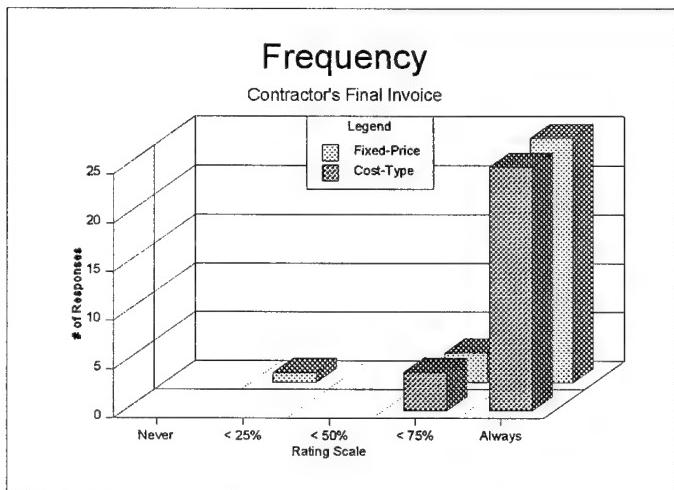


Figure 27.

Fixed-Price

Range: < 25% to Always.

Mean: 4.79 (75% +)

Median: 5 (Always)

Cost-Type

Range: < 75% to Always.

Mean: 4.86 (75% +)

Median: 5 (Always)

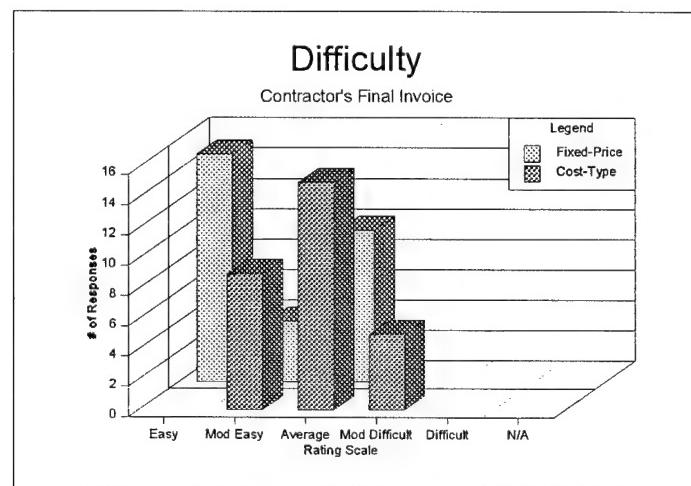


Figure 28.

Assessment: This action is required on all contracts unless the contract does not require submission of an invoice for payment. The contractor is required to submit a final invoice promptly upon completion of the contract but no later than one year from the completion

date. The submission of the Final Invoice is important if the payment amount is subject to contract settlement actions. Figure 27 shows that this task is performed almost always for both contract types.

The difficulty of this task as it applies to contract closeout can be attributed to a few factors: (i) the time-frame the contractors have to submit their final invoice, (ii) the accuracy of the final invoice, and (iii) the possible ramifications of the final invoice (e.g., payment to the Government of any refunds, rebates or credits). The responses shown in Figure 28 indicate that this task is moderately easy for Fixed-Price contracts and of average difficulty for Cost-Type contracts.

15. Contract Funds Review.

Figures 29 and 30 show the frequency and difficulty of performing a contract funds review and recommending deobligation of any excess funds.

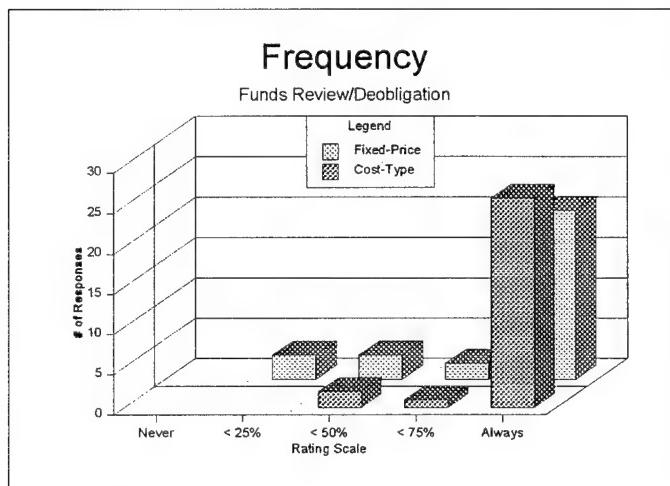


Figure 29.

Fixed-Price

Range: < 25% to Always.

Mean: 4.41 (75% +)

Median: 5 (Always)

Cost-Type

Range: < 50% to Always.

Mean: 4.83 (75% +)

Median: 5 (Always)

Fixed-Price

Range: Easy to Average.

Mean: 2.17 (Mod. Easy +)

Median: 2 (Mod. Easy)

Cost-Type

Range: Easy to Difficult.

Mean: 3.31 (Average +)

Median: 4 (Mod. Difficult)

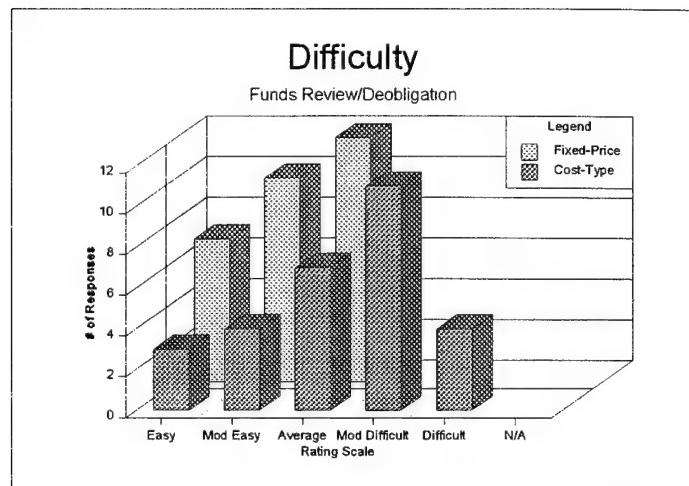


Figure 30.

Assessment: This task should be performed as part of every contract closeout. The results shown in Figure 29 indicate that funds review and deobligation of excess funds recommendations occur almost always for both contract types.

The difficulty with performing this task is a function of (i) the accuracy of the obligation and expenditure data on hand at the buying office, administration office and paying office, and (ii) the degree of reconciliation required to balance the accounts. The responses shown in Figure 30 indicate that this task was assessed to be moderately easy for Fixed-Price contracts while Cost-Type contracts were rated as moderately difficult. The difference may be attributed to the greater degree of financial activity and audit required to reconcile the financial accounts of a Cost-Type contract vice a Fixed-Price contract.

C. DATA ANALYSIS

Contract closeout is often a forgotten and neglected part of the contract administration process. The contract closeout process helps to insure that the Government's interests have been protected. The process attempts to resolve any contractual concerns and assures all contract requirements have been fulfilled. It encompasses many aspects and issues embodied within the contract. The fifteen steps involved in this process are essential elements of contract administration that were designed to uphold the Government's contractual rights.

The results of the questionnaire revealed some subtle differences between the closeout of Fixed-Price contracts and Cost-Type contracts. Most all of the closeout procedures (except for Termination Docket completed) were rated higher on both frequency and difficulty for Cost-Type contracts. This would connote that Cost-Type contracts are more complex contractual vehicles that require a higher degree of administration. However, the FAR does not distinguish between the contract types when delineating the procedures for contract closeout. The only major distinction is in the recommended time frames of contract closure action for Firm-Fixed-Price contracts versus contracts that require settlement of indirect rates.

There were several closeout procedures that had similar responses for both Fixed-Price and Cost-Type contracts. The disposition of Classified Material, Final Royalty Report cleared, no outstanding VECPs, Plant Clearance Report cleared, Property Clearance Report cleared and Termination docket completed all showed comparable difficulty ratings. The occurrence of these procedures depends on the applicability of the requirement to the

individual contract. These results appear to be valid since these actions are not contingent upon contract type.

There are several closeout procedures that are not applicable to Firm-Fixed-Price contracts if the results that included Fixed-Price Incentive contracts in the Fixed-Price category were discounted. Because Firm-Fixed-Price contracts do not involve pricing actions for contract closeout, the following actions are not required:

- * Interim/Disallowed costs settled,
- * Price Revision completed,
- * Prior Year Indirect Cost Rates settled, and
- *Contract Audit conducted.

Taking this into account, a Firm-Fixed-Price contract should theoretically be easier to closeout than a Cost-Type contract. The questionnaire responses substantiate this claim. The results for Fixed-Price contracts show a slightly lower level of difficulty in most closeout procedures and a significantly lower level in several others.

The Cost-Type contract results for frequency and difficulty ratings provided some revealing information. As previously stated, almost all of the closeout actions were performed more frequently and assessed to be more difficult for Cost-Type contracts. Most notable are the four areas that were rated significantly higher in difficulty than the others;

- * Settling all interim or disallowed costs,
- * Completing all price revisions,
- * Settling prior-year indirect cost rates, and
- * Completing contract audits.

All four areas were rated at least one level greater for the degree of difficulty. Table 2 may provide some insight into the reasons why these areas were deemed more difficult.

Closeout Action	PCO	ACO	DCAA	DFAS	Contractor
Disposition of Classified Material.		✓			
Final Patent Report Cleared.		✓			
Final Royalty Report Cleared.		✓			
No outstanding VECP's.		✓			
Plant Clearance Report Received.		✓			
Property Clearance Report Received.		✓			
All Interim or Disallowed costs are settled.	✓	✓	✓		✓
Price Revision is completed.	✓	✓	✓		✓
Subcontracts are settled by the Prime Contractor.		✓			✓
Prior-year indirect cost rates are settled.		✓	✓		✓
Termination docket is completed.		✓			
Contract audits are completed.	✓	✓	✓		
Contractor's closing statement is completed.		✓			✓
Contractor's Final Invoice is submitted.		✓			✓
Funds review/Deobligation of excess funds recommended.	✓	✓		✓	

Table 2. Participants Involved in Contract Closeout Actions.

Table 2 delineates the player(s) involved for each contract closeout action. The overall responses indicated that those actions in which the ACO was the only individual involved were rated to be of moderate ease. More importantly, these areas were assessed as the least difficult tasks of all fifteen. This may be due to the fact that since the ACO is the sole executor of the action and does not have to rely on the interaction of other individuals, the task would be perceived to be easier than one which requires input/action from another organization.

There were four areas that were rated significantly more difficult for Cost-Type contracts versus Fixed-Price contracts. (Interim or Disallowed Costs settled, Price Revision completed, Prior-year indirect cost rates settled, and Contract audits completed). These areas had three or more organizations involved with performing the particular action. DCAA and the ACO were common participants in these four closeout actions. These results are consistent with the findings of previous audit reports and indicate that these particular areas remain the “roadblocks” to efficient and effective contract closeout.

DCAA plays a major role in facilitating the contract closeout of Cost-Type contracts. The review, audit and settlement of interim or disallowed costs and prior-year indirect rates must be accomplished before final payment can be made. Price revisions and contract audits may also factor into the process. Any delay on the part of DCAA in fulfilling their audit responsibilities could adversely affect the closeout process. Additionally, these audit responsibilities are inherently time-consuming and complex, both factors which add to the difficulty in performing contract closeout.

The contractor is also involved in expediting the closeout process. Untimely submission of proposed final overhead rates, inaccurate data and erroneous invoices all preclude the ACO from executing the closeout process in a timely and efficient manner. These factors could provide the stimulus for the respondents to rate those closeout areas with contractor involvement more difficult than average.

D. FOLLOW-ON QUESTIONS

The following questions were posed to the individuals who assessed the frequency and difficulty of the closeout tasks. These questions were designed to gain insight into the current perception of the contract closeout process among the organizations that perform this process and to amplify and expand on some of the factors that inhibit the process.

1. What priority does the Contract Closeout process receive at your organization ?

Many of the prior audit reports stated that the contract closeout process was a low priority within the organization. Low priority was one of the factors that led to untimely closeout actions. The purpose of this question was to assess what the current management attention of the closeout process is within the organization.

Responses: 55% "The Highest" priority.

17% One Full-Time employee dedicated to the process.

14% High.

14% Average.

Analysis: Contrary to the previous findings, the results indicate that the priority assigned to the contract closeout process has improved. Many of the Defense Plant Representative

Offices stated that contract closeout "is a key element of their Strategic Performance Plan."

Other offices said that their organizations are assigned specific goals with closeout actions reported monthly to Headquarters. These results indicate that the contract closeout process no longer appears to be a neglected aspect of contract administration as it once was; instead, its significance within the overall scheme of contract administration has been elevated to a level commensurate with its importance. The magnitude of the adverse impacts of untimely contract closeout actions were probably the impetus behind the increased attention given to contract closeout. The Government can not afford to waste any of its valuable resources.

2. Does your organization utilize any internal controls to facilitate the contract closeout process ?

Without a specific internal control system, management would not be able to maintain visibility on the status of overaged contracts and the steps that remain outstanding in the closeout process. The previous audit reports stated that many organizations did not have effective internal controls in place to assist in the management of the closeout process.

Results: 86% Detailed Management Information System.

 11% Limited Information System.

 3% None.

Analysis: These results are not consistent with the results of prior audit findings which stated the lack of internal controls as a reason for untimely contract closeout. The vast majority of respondents indicated that their organization possessed some type of management information system that can provide detailed data concerning the status of overaged contracts. Many of these systems have real-time information capability that can retrieve the pertinent status of

closeout actions. A small portion of the respondents had some type of simplistic data base system in place that provided limited information.

These results would indicate that there is an effort on the part of the organization to institute effective measures to monitor and control the contract closeout process. This finding provides proof that the management of organizations which perform contract closeout are no longer blind to the status of overaged contracts within their purview. It appears the prior audit results were the catalyst that prompted the initiative to ensure management has the appropriate data to properly oversee the closeout process.

3. What specific area(s) impede your ability to closeout a contract within the prescribed time frames ?

This question was asked in order to identify those areas that hinder the closeout process. Additionally, this would identify the choke-points in the process. Possible corrective action or process improvements can then be identified and implemented.

Results: 42% Contractor caused delay.

 31% DCAA.

 14% Staffing.

 8% DFAS.

 5% Other.

Analysis: These responses are consistent with the prior audit report findings. The contractor and DCAA remain the foremost obstacles to the timely closeout of contracts. Many respondents reiterated identical viewpoints regarding contractor caused delays. Delays in contractor invoice submittal, errors in invoices that cause rejection, untimely submittal of

proposed overhead rates and low priority in providing supporting data were common reasons given for this response. Poor cooperation on the part of the contractor adversely impacts the contract closeout process and frustrates the ACO who is trying to execute this process effectively.

DCAA still contributes to untimely contract closeout. The results validate prior audit findings (although the percentages indicate their adverse impact may be declining). The principal reasons given were the backlog, delay and length of overhead rate negotiations and cost-incurred audits. Since DCAA is an integral player when it comes to the audit of Cost-Type and Fixed-Price Incentive contracts, any delay on their behalf would cause major perturbations in the contract closeout process.

Other responses included the lack of personnel and/or qualified personnel, problems with DFAS processing invoices and slow responses by the PCO concerning disposition or other instructions.

4. How can these areas be improved ?

This question provided respondents an opportunity to expand on their ideas for process improvement. Obviously the recommended improvements would coincide with the areas they felt were impediments to the process. The responses could be evaluated based on the marginal benefit provided to the process.

Responses: The respondents provided a myriad of recommendations. Some of the most notable are provided below:

* “Establish a joint DPRO (Cognizant Contract Administration Office)/Contractor Team to work and expedite all contract closeout issues.”

- * “Train individuals in the contracting workforce to be closeout specialists vice overall generalists.”
- * “Establish incentives for the contractor to expedite the closeout process.”
- * “Request DCAA overhead audits concurrent with final voucher approval.”

Analysis: The teaming concept is currently an issue that has great merit and is consistent with many acquisition reform initiatives. A CAO/Contractor team would permit the free flow of information between each organization and establish common priorities for the requisite actions of contract closeout. This would also ensure proactive measures are taken immediately upon physical completion of a contract to facilitate timely closeout. The adverse effects of untimely closeout should be mitigated to a tolerable level.

The concept of having a closeout specialist is debatable. One can argue that there are various aspects of contract administration with specialists. Quality Assurance, Property Administration, Production Specialists and Price Analysts all perform specific functions of the contract administration process. A contract closeout specialist could certainly be a subject matter expert when it comes to working the nuances of the contract closeout process. However, since the closeout process encompasses routine contract administration actions, the need for a specialist may not be warranted. A contract closeout specialist may be a solution for a short-term problem but in order to have an effective workforce, a general knowledge of all facets of contract management would be more practical.

Providing incentives for the contractor to facilitate the closeout process is another controversial issue. The contractor is already required (either by the FAR or contractual clauses) to provide certain information or reports necessary for proper contract closeout.

Positive incentives in the form of monetary remuneration to submit these requirements in a timely matter should not be considered. A more appropriate incentive may be one with negative ramifications such as reduced profit or fee. This may be an effective tool to motivate the contractor to comply with these closeout requirements.

Concurrent audit by DCAA of the proposed overhead rates and the final voucher should promote the timely completion of contract closeout. The contractor must submit final overhead data which then must be audited, negotiated and approved before the final voucher can be submitted for audit. Although the audit and negotiation of final overhead rates is a lengthy process that sometimes takes years to complete, concurrent audit of the final voucher can potentially accelerate the total time required to closeout a Cost-Type contract. Since the FAR allows 36 months to closeout Cost-Reimbursement/Fixed-Price Incentive contracts, the concurrent audit concept should be considered as a viable means to foster timely closeout.

E. DCAA AND CONTRACTOR REMARKS

The researcher contacted various DCAA offices and contractor activities in order to obtain some candid replies concerning the findings of certain areas in the questionnaire. The specific area addressed was the perception among the ACOs that DCAA and the contractor were the primary inhibitors to the contract closeout process.

All the DCAA offices recognized the importance of supporting the contract closeout process with timely overhead rate negotiations. Every organization said this issue has been given high priority, however, field-pricing reports and lack of personnel continue to hamper their efforts. Until there are additional manpower resources, the backlog of DCAA closeout audits should remain constant.

The responses from the contractors were varied. Many professed their complete support to facilitate the contract closeout process while others expressed luke warm sentiments. Many contractors claimed there is more importance placed on managing current active contracts and potential awards vice those that have already been physically completed. Although most agreed that the process was necessary, many felt it is cumbersome and complex. Additionally, a small portion felt DCAA was overbearing while executing their audit responsibilities.

F. SUMMARY

This chapter presented and analyzed the data obtained from a questionnaire conducted by the researcher. The frequency and difficulty of all fifteen contract closeout steps were assessed and analyzed for both Fixed-Price and Cost-Type contracts. In addition, follow on questions were addressed in order to determine the current priority of the contract closeout process, the level of internal controls used to facilitate management of this process, areas that impede timely contract closeout and areas that can be implemented to improve the process. Chapter V will provide conclusions, recommendations, answers to research questions and recommendations for further research.

V. CONCLUSIONS AND RECOMMENDATIONS

A. INTRODUCTION

Proper documentation and sound contract administration will make contract closeout easier to accomplish and faster to complete. Those ACOs who perform contract closeout rely on many other agencies to assist them throughout the process. A streamlined contract closeout process will mitigate the potential adverse effects of untimely contract closeout actions. Agencies will be better equipped to manage and execute their budgets. Timely identification and recovery of unliquidated obligations will permit reprogramming of funds to other valid requirements. Overpayments to the contractor will be quickly recouped, thus decreasing the interest costs to the Government. Dormant GFP will be screened and reutilized on other contracts. Backlogs of physically completed contracts awaiting closeout actions will be reduced to acceptable limits which would also lessen the likelihood of legal action and the perception of potential fraud.

A streamlined contract closeout process is in consonance with the Guiding Principles for the Federal Acquisition System. The individuals who perform contract closeout will be empowered to exercise personal initiative and make sound business judgments in providing the best value service to their customer. The public's trust will be upheld, administrative operating costs will be minimized and the best interests of the Government will be preserved.

B. CONCLUSIONS

The scope of this research effort has led to several conclusions concerning the management and execution of the contract closeout process as it is currently performed.

Conclusion 1. The management and priority of the contract closeout process have improved, however, there are still some significant “roadblocks” that hinder timely contract closeout execution.

The audit reports from 1985 through 1992 all cited low priority and, to some extent, poor management as primary reasons that cause untimely contract closeout. The adverse impacts of untimely contract closeout provided the motivation to elevate this issue to the forefront of management attention. The responses to follow-on questions indicate that the priority assigned to the contract closeout process has improved in the majority of organizations. The implementation of closeout goals and incorporating contract closeout as a key element of the organization's strategic performance plan are positive steps that elevate the importance of this process. In addition, improved internal controls have been instituted in order to monitor and control the contract closeout process. Management in the majority of organizations questioned now possess the requisite information to properly oversee the closeout process. However, some of the respondents stated they are constrained by the lack of personnel and/or qualified personnel, and many experience problems when interacting with the other agencies involved in the closeout process. These “roadblocks” continue to impede the effective and efficient execution of contract closeout.

Conclusion 2. The organizations that perform contract closeout rated the areas that involve DCAA and/or contractor action/input as more difficult than the areas in which the ACO is the sole executor of the action.

The responses to the questionnaire which asked each agency to rate the frequency and

difficulty of the fifteen contract closeout steps clearly showed that those closeout areas which involve the contractor or DCAA were rated higher in difficulty than the areas involving only the ACO. The follow-on questions also reiterated this finding. Contractor and DCAA caused delays accounted for 73% of the responses as the specific area(s) that impede the organization's ability to closeout a contract within the required time frames. These perceptions should be considered valid since it is the ACO that is responsible for the execution of the contract closeout process and therefore is the individual who is most familiar with the details and requirements of the process.

Conclusion 3. Cost-Type contracts (including Fixed-Price-Incentive contracts) are more difficult to closeout than Fixed-Price contracts.

The questionnaire responses showed that the difficulty associated with the closeout of a Cost-Type contract was higher in all but one of the closeout procedures than a Fixed-Price contract. The four closeout tasks that are applicable only to Cost-Type contract closeout (Interim/Disallowed costs settled, Price Revision completed, Prior year Indirect Cost Rates settled, and Contract Audit conducted) are the main causes of the higher level of difficulty. Because these procedures are inherently complex and time-consuming, they remain obstructions to the timely closeout of Cost-Type contracts. Additionally, the difficulty associated with completing these four areas jeopardizes the goal of achieving closeout within the required FAR time frame.

Conclusion 4. The actions and timeliness of the contractor can either facilitate or hinder the contract closeout process.

The contractors play a major role in expediting the contract closeout process. They are primary participants in seven of the contract closeout actions and secondary participants in another seven actions. The only step with which they are not directly involved is Funds review/Deobligation of excess funds. The responses to the follow-on questions cited contractor caused delay as the number one impediment to timely contract closeout. Untimely submission of overhead rates, erroneous data and lack of communication or cooperation with other agencies all preclude the ACO from executing the closeout process in a timely and practical manner. Conversely, any contractor that provides timely and accurate data to the ACO will greatly facilitate the process.

Conclusion 5. There are no controls in place to insure the contractor fulfills their requirements for timely contract closeout.

As the process stands now, there are no incentives or disincentives for the contractor to support the timeliness of the contract closeout process. The contractor acts according to its own volition. The responses of the contractors polled showed a vast range of support for the closeout process. In addition, the responses to the follow-on questions provided by those organizations that perform contract closeout indicate there should be controls in place that motivate the contractor to provide the Government with accurate and timely data in order to expedite this process. The Government must clearly delineate the contractor's responsibility

in the closeout process and establish effective controls that insure they fulfill this responsibility.

Conclusion 6. Time-frames for certain closeout actions do not exist and others are incompatible with the required time-frames for contract type.

While assessing the frequency and difficulty of the fifteen contract closeout factors, it became apparent that many of these steps lacked any prescribed time-frame for completion while others were inconsistent with the FAR closeout time-frames established for contract type. For example, the prescribed time-frame for a Firm-Fixed-Price contract closeout is six months. If the contractor receives a Termination for Convenience notice (i.e. the contract is deemed physically complete), then they have up to one year to submit a settlement claim. Should the full time elapse, the contract would be considered overaged through no fault of the ACO's.

This matter is further illustrated by examining the closeout actions for a Cost-Type contract. The contractor is required to submit the final invoice within one year of contract completion. However, before a contractor can submit the final invoice, the proposed final overhead rates must be submitted (within 90 days after end of contractor's fiscal year), audited and negotiated. Depending on when in the contractor's fiscal year the contract is completed, the contractor may have from three months to 15 months to submit the overhead data. Audit and negotiation time-frames for overhead rates are not delineated in the FAR. The total time for these steps make the one year requirement for final invoice submittal unrealistic. These inconsistencies may needlessly complicate the closeout process.

Conclusion 7. The contract closeout process requires a great deal of coordination between various activities.

The contract closeout process may involve up to six different organizations to rectify an issue. The PCO, ACO, DFAS, DCAA, contractor and subcontractors may all provide input to the closeout process. The ACO must ensure all parties are working in unity with one another. This can certainly be a daunting task, especially if there is a conflict over an issue. The ACO must shoulder the consequences of the process' outcome regardless of the level of support received. This adds to the overall difficult and cumbersome nature of the process.

C. RECOMMENDATIONS

Based on the conclusions of this research, the following recommendations are made.

Recommendation 1. Accept the contractor's independently audited and certified Indirect Cost Rates.

The submission, audit and approval of indirect rates is complex and time consuming. This action was rated the most difficult of the 15 contract closeout steps for Cost-Type contracts. The audit of indirect rates involves DCAA and the contractor; the top two responses for the area(s) that impede the contract closeout process.

Much like Certified Cost and Pricing Data, this recommendation espouses that the contractor bear the burden of this task by having the overhead rates audited by an independent accounting agency and certified to be current, accurate and complete. A statement addressing allowability, allocability and reasonableness would also be included. The Government would retain audit rights for a specified period and the contractor would be liable for any excess payments received due to erroneous certified rates.

Transferring this task to the contractor accomplishes two objectives: (i) the contractor is motivated to submit timely and accurate rates because final payment now hinges on an action for which they are directly responsible, and (ii) the Government does not have to contend with resource allocation and constraint issues for overhead rate audits and negotiations. Additionally, DCAA can concentrate on field-pricing audits and final invoice audits. In theory, this recommendation should help expedite the contract closeout process. One of the main obstacles to the closeout process would be replaced by a viable alternative that should not restrict the Government's ability to protect its best interests.

Recommendation 2. Establish effective controls that provide an incentive for contractors to achieve timely contract closeout.

The Government must first establish a comprehensive list of requirements for which the contractor is responsible during the closeout process. These criteria can be incorporated into the contract or included in the FAR. Once these conditions have been promulgated, the ramifications of the contractor's failure to comply with these requirements must be addressed. Specific consequences may include reductions in contractor profits, monetary penalty and/or reduction in final indirect rates. Whatever sanction is selected, it must be penal enough so the contractor avoids any action that would thwart the closeout process. Once contractors understand their actions or inactions will adversely impact their financial posture, the impetus to assist the process will be in place.

Recommendation 3. Make Funds Review/Deobligation of Excess Funds a priority in the contract closeout process.

A review of the funding status and recommendation for deobligation of excess funds should be accomplished for all contracts. The results of the questionnaire indicated that this was not the case. Failure to perform this task can potentially lead to numerous monetary problems.

Timely funds review and deobligation of any excess funds will minimize the amount of unliquidated obligations in the Government's financial accounts. It will also permit reprogramming these funds to valid unfunded requirements. The potential to recoup millions of dollars should be a paramount concern for all contract managers, especially in today's austere funding environment.

Proper contract management dictates that this closeout step should be one of the first performed. The ramifications of neglecting this step are too great. The overall importance of funds review and deobligation of excess funds must be emphasized to all individuals involved in the closeout process.

Recommendation 4. Establish specific time-frames for each step/factor of the Contract Closeout process based on contract type and dollar value.

The majority of the contract closeout steps do not have any prescribed time-frames for execution. The contractor and Government attempt to accomplish all the applicable tasks within the prescribed time limit promulgated for contract type. This complicates the process and contributes to the untimely closeout of contracts.

The Government should establish realistic time standards based on contract type and dollar value for each contract closeout factor. The impact of the Federal Acquisition Streamlining Act should also be considered (e.g., the Small Purchase threshold regardless of contract type). This would enable the contractor and Government to effectively plan throughout the process and commit the requisite resources to the urgent tasks. Realistic time-frames will also facilitate the closeout process. Each player in the process would be aware of the performance requirement and should execute accordingly.

Recommendation 5. Create a "teaming" arrangement with the contractor to facilitate closeout procedures.

Establishing a teaming arrangement with the contractor will help facilitate all aspects of contract management. The free flow of information that emanates from this type of arrangement would expedite certain tasks in the closeout process. Additionally, up to date knowledge of the contractor's costs and rates would be factors the ACO can consider when deciding the magnitude of contract audits and reviews. Issues that stall the process can be jointly discussed and resolved. The importance and priority of the contract closeout process would be the same for both the contractor and Government. A teaming concept should promote timely and effective contract closeout.

Recommendation 6. Perform all actions possible that can be accomplished during contract performance in order to facilitate the closeout process once the contract has become physically complete.

The fifteen contract closeout steps typically commence once the contract is physically completed. This practice may result in the untimely and inefficient execution of the contract closeout process. Taking proactive measures during contract performance would ensure potential perturbations are minimized and promote closeout expediency.

There are several closeout steps that lend themselves to proactive measures during contract performance. The following examples illustrate certain actions the contracting officer can take to expedite contract closeout:

- * Require the contractor to return or destroy all Classified Material immediately after it is no longer needed for contract performance. This would ensure proper disposition was accomplished at the first available opportunity and not delayed until the contract has been completed.
- * Establish a date, 90 to 120 days prior to contract completion, for the contractor to submit preliminary Government Property inventory schedules. This action would allow the Government property administrator ample time to identify and resolve property issues prior to providing disposition instructions upon completion of the contract.
- * Request the contractor provide interim statements concerning the status of Patent Rights, Royalties and VECPs 90 to 120 days prior to contract completion. The contractor would be allowed to submit amended reports should the status of these areas change from the time of original submission to contract completion.
- * Review individual Cost-Type contracts to determine if it meets the criteria for Quick Closeout; utilize the Quick Closeout procedures whenever practical in order to reduce the magnitude of indirect rate audits.

D. SUMMARY AND REVIEW OF RESEARCH QUESTIONS

In order to accomplish the objectives of this thesis, fundamental research questions were developed. The responses to these questions will now be provided. The subsidiary questions will be answered first, followed by the primary research question.

Secondary Question 1: What are the current procedural requirements for contract closeout ?

The current procedural requirements for contract closeout were provided in Chapter II. The administrative closeout process commences once the cognizant contract administration office has evidence a contract is physically complete. An initial contract funds status review is performed to identify excess funds that are available on the contract. The ACO then ensures the applicable steps listed in FAR 4.804-5 are completed. After these actions have been verified, the ACO prepares a Contract Completion Statement, DD Form 1594. The ACO forwards the signed original to the contracting office for placement in the contract file and a signed copy is placed in the contract administration file. The final step of the contract closeout process involves the storage and disposition of the contract files. The FAR states that agencies shall prescribe procedures for handling, storing and disposing of contract files. The FAR also specifies retention periods for certain contractual documents.

The FAR does not distinguish between contract types when delineating the procedures for contract closeout. The only major distinction is in the recommended time-frames of closure action for Firm-Fixed-Price contracts versus contracts that require settlement of indirect rates.

The contract closeout process may involve up to six different organizations to rectify an issue. Each organization may be required to take action or provide input in order to facilitate the process. Communication and coordination are required to aid the process.

Secondary Question 2. What are the primary factors affecting timely and proper contract closeout ?

The factors that affect timely and proper contract closeout were addressed in Chapters III and IV. Virtually every audit report from 1985 to 1992 evaluated the reasons why the closeout process has gone awry. The following reasons were identified as the main causes of untimely and improper contract closeout:

* Inaction by the Contractor. Contractors contributed to delayed contract closeout for all types of contracts. Delays were found in submitting overhead data, negotiating overhead rates, submitting invoices and responding to queries from contracting offices. The contractor was identified in the follow-on questions as the primary reason contracts are not closed out in a timely manner.

* Inaction by DCAA. Before any Cost-Reimbursement or Fixed-Price-Incentive contract can be closed out, DCAA must audit the year end overhead rates. Any delay in completing the audit will adversely impact the closeout process. Delays and backlogs of audits were found to be a common factor. The follow-on questions indicated inaction by DCAA is still a prevalent factor.

* Inaction by the ACO. The ACO is responsible for executing the majority of the closeout actions required by the FAR. Additionally, the ACO coordinates the actions of

various organizations involved in the closeout process. Any delay on the part of the ACO will ultimately delay contract closeout.

* Low Priority/Lack of Internal Controls. The audit reports indicated that the contracting offices generally gave the contract closeout process and required closeout actions low priority. Additionally, many contracting offices did not have a system for identifying actions needed to closeout individual contracts. These reasons were dispelled by the research questionnaire which found that the priority of contract closeout has been elevated to the forefront. Furthermore, the majority of the contracting offices had a detailed management information system in place to provide the requisite feedback to monitor and control the closeout process.

Secondary Question 3. What are the consequences to the Government for untimely contract closeout ?

Impacts of untimely contract closeout were addressed in Chapter III. Timely contract closeout is the primary step to ensure the Government's best interests are protected. Untimely contract closeout action(s) can potentially create a variety of adverse impacts upon the Government. Some of the detrimental impacts of delayed contract closeout are:

* Monetary Impact. The monetary impact of untimely contract closeout can be one of several outcomes: unliquidated obligations, negative unliquidated obligations and unnecessary interest costs. Unliquidated obligations are those unused and unneeded funds that remain on a physically completed contract after some portion of the obligated funds have been expended. These funds are lost if contract closeout actions delay deobligation until after

they have expired. Negative unliquidated obligations typically occur when the contractor is paid too much. Untimely contract closeout actions will permit negative unliquidated obligations to go unchecked. In conjunction with the adverse effects caused by negative unliquidated obligations, delayed contract closeout can unnecessarily increase interest costs to the U.S. Treasury if the excess payments to contractors are not recovered in a timely manner.

* Government Furnished Property. Delayed contract closeout can cause GFP to needlessly remain in the contractors' possession. This increases the potential for property loss, damage or abuse.

* Increased Backlog. Delayed contract closeouts typically create work backlogs in contracting organizations. These backlogs can reduce efficiency and disrupt the organization's normal operations when management shifts resources to reduce the backlog.

* Fraud or Waste. Fraud or waste in individual contracts are often discovered during contract closeout. Detecting and resolving problems such as contractor cost mischarging and defective pricing may be delayed when closeout actions are late.

Secondary Question 4. What marginal utility/benefit would the Government obtain if contracts were closed out in a timely manner ?

This question was addressed throughout Chapters III and IV. The marginal utility/benefits are directly linked to reducing or eliminating the adverse impacts of untimely contract closeout. Accordingly, timely contract closeout actions, such as deobligation of excess funds, would allow reprogramming funds to satisfy unfunded budget contingencies.

Timely funds review can also identify and correct the problems associated with negative unliquidated obligations before they reach monumental proportions. The potential to save millions of scarce funding dollars is great. Prompt contract closeout will also ensure GFP is quickly returned to Government control and not retained in the contractor's plant where the potential exists for loss, destruction or abuse. Timely contract closeouts will reduce the backlog in contracting organizations. The organization's normal administrative function will operate in a more efficient and effective manner. Lastly, the potential of fraud or waste in an individual contract will be mitigated through timely closeout actions.

Primary Question. What are the principal factors that affect the management of the contract closeout process and how can improvements be implemented to streamline the process ?

The first part of this question was touched upon in Secondary Question number 2. The primary factors that affect timely and proper contract closeout are also some of the issues that affect the management of the contract closeout process.

Contract managers must deal with a myriad of issues on a daily basis: personnel, funding, training, priority of work assignments, interaction with other agencies and customer satisfaction are some of their primary concerns. Sound management practices entail balancing constrained resources to meet the organizational goals while effectively dealing with these issues. Management of the contract closeout process encompasses all these factors. A priority for contract closeout must be established among the multitude of other contract administration functions. Appropriate internal controls must be in place to monitor and

control this process. An adequate number of trained personnel must be available to execute timely contract closeout. Proper communication and coordination between the various agencies are essential elements of the contract closeout process. Effective and efficient contract closeout management will balance all these factors. The manager who neglects or diminishes the importance of any of these factors risks jeopardizing the organization's productivity.

The second part of this question deals with implementing improvements to streamline the process. The Recommendations section addressed some possible streamlining improvements.

One of the first steps to finding areas that can be streamlined is to assess those areas that impede the process. The frequency and difficulty questionnaire plus the follow-on questions found some potential "bottlenecks" in the closeout process. The audit and negotiation of prior-year indirect rates was considered to be a major obstruction to timely contract closeout. Allowing the contractor to submit independently audited indirect rates would drastically expedite the process. Major delays and manpower requirements needed to perform this task would be minimized. Contract administration personnel would be afforded the opportunity to better manage and facilitate the remaining closeout steps.

Other process improvements include establishing contractor requirements for the contract closeout process and developing prescribed time standards for each closeout task. These initiatives would eliminate some of the confusion that currently exists. Both the contractor and Government would be cognizant of their respective duties and the associated

time-frames to complete them. The overall affect of these recommendations would be a streamlined process that operates efficiently and effectively.

E. AREAS FOR FURTHER RESEARCH

The contract closeout process has been examined over the past decade. Current contracting reforms and process action teams have assessed many aspects of contract management. Specific areas that merit further research include:

* The benefits and efficiencies derived from a Government and contractor teaming or partnering arrangement. Contract closeout requires a great deal of Government interaction with the contractor. A contract management teaming arrangement would facilitate this interaction for all administrative actions. An analysis of such an arrangement can be compared and contrasted to the current effects of dealing in an “us versus them” relationship.

* The value added of DCAA overhead audits for contract closeout. The audit of contractor overhead rates is complex and time consuming. A cost-benefit analysis to study the difference between the actual proposed overhead costs versus the final negotiated overhead costs compared to the manpower resources expended to audit and negotiate the rates would determine the value of this process. The objective would be to determine the threshold where overhead rate audits provide a significant decrease in costs.

APPENDIX QUESTIONNAIRE RESPONSES

FIXED-PRICE CONTRACTS - FREQUENCY

	Scale				
	1	2	3	4	5
Disposition of Classified Material	5	21	3	0	0
Final Patent Report Cleared	11	14	4	0	0
Final Royalty Report Cleared	21	8	0	0	0
No outstanding VECPs	23	3	1	2	0
Plant Clearance Report Received	4	8	9	5	3
Property Clearance Report Received	0	10	5	9	5
All Interim or Disallowed Costs Settled	20	6	3	0	0
Price Revision Completed	22	5	2	0	0
Subcontracts settled by Prime Contractor	10	9	5	3	2
Prior-year Indirect Cost Rates Settled	24	5	0	0	0
Termination Docket Completed	5	20	4	0	0
Contract Audits Completed	21	5	3	0	0
Contractor's Closing Statement Completed	22	4	3	0	0
Contractor's Final Invoice Submitted	0	1	0	3	25
Funds Review/Deobligation of Excess Funds	0	3	3	2	21

FIXED-PRICE CONTRACTS - DIFFICULTY

	Scale					
	1	2	3	4	5	N/A
Disposition of Classified Material	3	11	8	1	1	5
Final Patent Report Cleared	11	4	1	2	0	11
Final Royalty Report Cleared	3	4	1	0	0	21
No outstanding VECPs	0	4	2	0	0	23
Plant Clearance Report Received	11	8	3	3	0	4
Property Clearance Report Received	12	9	5	3	0	0
All Interim or Disallowed Costs Settled	0	2	7	0	0	20
Price Revision Completed	0	7	0	0	0	22
Subcontracts settled by Prime Contractor	8	11	0	0	0	10
Prior-year Indirect Cost Rates Settled	0	0	3	2	0	24
Termination Docket Completed	3	16	2	1	2	5
Contract Audits Completed	3	5	0	0	0	21
Contractor's Closing Statement Completed	2	5	0	0	0	22
Contractor's Final Invoice Submitted	15	4	10	0	0	0
Funds Review/Deobligation of Excess Funds	7	10	12	0	0	0

COST-TYPE CONTRACTS - FREQUENCY

	Scale				
	1	2	3	4	5
Disposition of Classified Material	5	15	7	2	0
Final Patent Report Cleared	0	7	5	13	4
Final Royalty Report Cleared	8	7	6	6	2
No outstanding VECPs	20	4	3	2	0
Plant Clearance Report Received	0	12	4	3	10
Property Clearance Report Received	0	6	3	4	16
All Interim or Disallowed Costs Settled	12	7	6	1	3
Price Revision Completed	16	12	1	0	0
Subcontracts settled by Prime Contractor	7	5	13	4	0
Prior-year Indirect Cost Rates Settled	0	7	13	3	6
Termination Docket Completed	7	18	4	0	0
Contract Audits Completed	0	3	3	5	18
Contractor's Closing Statement Completed	0	2	3	5	19
Contractor's Final Invoice Submitted	0	0	0	4	25
Funds Review/Deobligation of Excess Funds	0	0	2	1	26

COST-TYPE CONTRACTS - DIFFICULTY

	Scale					
	1	2	3	4	5	N/A
Disposition of Classified Material	4	10	5	3	2	5
Final Patent Report Cleared	6	8	9	6	0	0
Final Royalty Report Cleared	7	7	4	3	0	8
No outstanding VECPs	2	5	2	0	0	20
Plant Clearance Report Received	10	8	4	4	3	0
Property Clearance Report Received	11	11	4	3	0	0
All Interim or Disallowed Costs Settled	0	0	6	11	0	12
Price Revision Completed	0	0	3	4	6	16
Subcontracts settled by Prime Contractor	0	3	12	4	3	7
Prior-year Indirect Cost Rates Settled	0	0	6	11	12	0
Termination Docket Completed	7	11	4	0	0	7
Contract Audits Completed	3	7	15	4	0	0
Contractor's Closing Statement Completed	6	4	9	10	0	0
Contractor's Final Invoice Submitted	0	9	15	5	0	0
Funds Review/Deobligation of Excess Funds	3	4	7	11	4	0

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